K2 INC
Form 10-Q
August 05, 2005

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 June 30, 2005

Commission File No. 1-4290

K2 INC.

(Exact name of registrant as specified in its charter)

Delaware **(State of Incorporation)**	**95-2077125** **(I.R.S. Employer Identification No.)**
5818 El Camino Real **Carlsbad, California** **(Address of principal executive offices)**	**92008** **(Zip Code)**

Registrant s telephone number, including area code (760) 494-1000

Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report:

Not applicable

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes x No ¨

At July 31, 2005, there were 47,598,286 shares of Common Stock ($1.00 par value) outstanding.

PART - 1 FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS

CONSOLIDATED CONDENSED STATEMENTS OF INCOME (UNAUDITED)

(Thousands, except per share figures)

	Three months ended June 30		Six months ended June 30	
	2005	2004	2005	2004
		(Unaudited)		
Net sales	$ 301,425	$ 250,987	$ 619,716	$ 528,351
Cost of products sold	201,667	173,622	417,139	364,353
Gross profit	99,758	77,365	202,577	163,998
Selling expenses	54,502	41,566	113,217	83,613
General and administrative expenses	36,910	23,354	71,003	48,418
Operating income	8,346	12,445	18,357	31,967
Interest expense	7,285	3,210	14,538	6,512
Other income, net	(1,117)	(125)	(1,838)	(178)
Income before income taxes	2,178	9,360	5,657	25,633
Provision for income taxes	725	3,182	1,880	8,715
Net income	$ 1,453	$ 6,178	$ 3,777	$ 16,918
Basic earnings per share:				
Net income	$ 0.03	$ 0.18	$ 0.08	$ 0.48
Diluted earnings per share:				
Net income	$ 0.03	$ 0.16	$ 0.08	$ 0.43
Basic shares outstanding	46,216	35,273	46,196	34,894
Diluted shares outstanding	47,373	44,019	47,430	43,659

See notes to consolidated condensed financial statements.

CONSOLIDATED CONDENSED BALANCE SHEETS

(Thousands, except number of shares)

	June 30 2005	December 31 2004
	(Unaudited)	
Assets		
Current Assets		
Cash and cash equivalents	$ 21,450	$ 25,633
Accounts receivable, less allowances for doubtful accounts of $15,656 (2005) and $14,895 (2004)	264,844	369,914
Inventories, net	367,127	325,125
Deferred income taxes	20,868	29,709
Prepaid expenses and other current assets	28,151	22,775
Total current assets	702,440	773,156
Property, plant and equipment	284,189	272,959
Less allowance for depreciation and amortization	142,854	131,995
	141,335	140,964
Other Assets		
Goodwill	343,088	349,760
Tradenames	145,829	137,329
Other intangible assets, net	21,292	21,276
Deferred income taxes	7,506	7,506
Other	24,377	26,374
Total Assets	$ 1,385,867	$ 1,456,365
Liabilities and Shareholders Equity		
Current Liabilities		
Bank loans	$ 7,017	$ 31,490
Accounts payable	73,604	103,158
Income taxes payable	25,938	28,386
Accrued payroll and related	44,895	50,589
Other accruals	99,370	100,478
Current portion of long-term debt	19,123	35,074
Total current liabilities	269,947	349,175
Long-term pension liabilities	16,854	16,854
Long-term debt	274,004	250,812
Deferred income taxes	50,746	58,123
Convertible subordinated debentures	98,769	98,535
Commitments and Contingencies		
Shareholders Equity		
Preferred Stock, $1 par value, authorized 12,500,000 shares, none issued		
Common Stock, $1 par value, authorized 110,000,000 shares, issued and outstanding shares - 47,594,257 in 2005 and 47,543,108 in 2004	47,594	47,543
Additional paid-in capital	502,942	502,322
Retained earnings	150,335	146,558
Treasury shares at cost, 747,234 shares in 2005 and 2004	(9,107)	(9,107)
Accumulated other comprehensive loss	(16,217)	(4,450)
Total Shareholders Equity	675,547	682,866
Total Liabilities and Shareholders Equity	$ 1,385,867	$ 1,456,365

See notes to consolidated condensed financial statements

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS (Unaudited)

(Thousands)

	Six months ended June 30	
	2005	**2004**
	(unaudited)	
Operating Activities		
Net Income	$ 3,777	$ 16,918
Adjustments to reconcile net income from operations to net cash provided by operating activities:		
Depreciation and amortization	17,278	12,743
Deferred taxes	1,415	6,782
Changes in current assets and current liabilities	19,827	20,517
Net cash provided by operating activities	42,297	56,960
Investing Activities		
Property, plant & equipment expenditures	(17,308)	(14,258)
Disposals of property, plant & equipment	872	406
Purchase of business, net of cash acquired	(15,094)	(28,672)
Other items, net	1,651	(5,291)
Net cash used in investing activities	(29,879)	(47,815)
Financing Activities		
Borrowings under long-term debt	548,000	379,149
Payments of long-term debt	(540,525)	(391,942)
Net decrease in short-term bank loans	(24,473)	(3,526)
Exercise of stock options	397	4,091
Net cash used in financing activities	(16,601)	(12,228)
Net decrease in cash and cash equivalents	(4,183)	(3,083)
Cash and cash equivalents at beginning of year	25,633	21,256
Cash and cash equivalents at end of period	$ 21,450	$ 18,173

See notes to consolidated condensed financial statements.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

June 30, 2005

NOTE 1 Basis of Presentation

The accompanying unaudited consolidated condensed 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 statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six month periods ended June 30, 2005 are not necessarily indicative of the results that may be expected for the year ending December 31, 2005.

The consolidated condensed balance sheet at December 31, 2004 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

K2 Inc. (K2) reports its financial statements using a 13 week quarter ending on the last Sunday of March, June, September and December. For purposes of the consolidated financial statements, the end of each quarter is stated as of March 31, June 30, September 30 and December 31, respectively.

The interim financial statements should be read in connection with the financial statements in K2 s Annual Report on Form 10-K for the year ended December 31, 2004.

Certain prior year amounts have been reclassified to conform to the current year presentation.

NOTE 2 Recent Accounting Pronouncements

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 123 (Revised), *Share-Based Payment.* SFAS No. 123 (Revised) requires that companies recognize compensation expense equal to the fair value of stock options or other share based payments. The impact on K2 s net income will include the remaining amortization of the fair value of existing options currently disclosed as pro forma expense in Note 3 and is contingent upon the number of future options granted, the selected transition method and the selection of either the Black-Scholes or the binominal lattice model for valuing options.

On April 14, 2005, the SEC adopted a new rule that amended the compliance dates of SFAS No. 123 (Revised) to require implementation no later than the beginning of the first fiscal year beginning after June 15, 2005 (the year beginning January 1, 2006 for K2). Early adoption of SFAS No. 123 (Revised) is permissible. K2 is in the process of evaluating the use of certain option-pricing models as well as the assumptions to be used in such models. When such evaluation is complete, K2 will

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 2 Recent Accounting Pronouncements (Continued)

determine the transition method to use, the timing of adoption and the impact any change in valuation models might have.

In May 2005, the FASB issued SFAS No. 154, *Accounting Changes and Error Corrections*. SFAS No. 154 replaces APB Opinion No. 20, *Accounting Changes* and SFAS No. 3, *Reporting Accounting Changes in Interim Financial Statements*. SFAS No. 154 requires that a voluntary change in accounting principle be applied retrospectively with all prior period financial statements presented on the new accounting principle unless it is impracticable to do so. SFAS No. 154 also provides that a change in method of depreciating or amortizing long-lived non-financial assets be accounted for as a change in estimate effected by a change in accounting principle and that correction of errors in previously issued financial statements should be termed a restatement. SFAS No. 154 is effective for accounting changes and correction of errors made in fiscal years beginning after December 15, 2005. Early adoption of this standard is permitted for accounting changes and corrections of errors made in fiscal years beginning after June 1, 2005. K2 believes that implementing SFAS No. 154 should not have a material impact on its financial position and results of operations.

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NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 3 Stock Based Compensation

K2 currently applies the provisions of SFAS No. 123, *Accounting for Stock-Based Compensation,* which allows entities to continue to apply the provisions of Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees,* and related interpretations and provide pro forma net income and pro forma net income per share disclosures for employee stock option grants made as if the fair-value-based method defined in SFAS No. 123 had been applied. K2 has elected to continue to apply the provisions of APB Opinion No. 25 and provide the pro forma disclosure provisions of SFAS No. 123. As such, compensation expense for stock options issued to employees is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. Had compensation cost been determined based upon the fair value at the grant date for K2 s stock options under SFAS No. 123 using the Black-Scholes option pricing model, pro forma net income and pro forma net income per share, including the following weighted average assumptions used in these calculations, would have been as follows:

	For the three months ended June 30		For the six months ended June 30	
	2005	**2004**	**2005**	**2004**
	(Thousands, except per share data, percentage data and expected life)			
Net income as reported	$ 1,453	$ 6,178	$ 3,777	$ 16,918
Less: Total stock-based compensation expense determined under fair value based method for all awards, net of taxes	8,869	384	9,531	768
Net income (loss), adjusted	$ (7,416)	$ 5,794	$ (5,754)	$ 16,150
Earnings (loss) per share:				
Basic - as reported	$ 0.03	$ 0.18	$ 0.08	$ 0.48
Basic - pro forma	$ (0.16)	$ 0.16	$ (0.12)	$ 0.46
Diluted - as reported	$ 0.03	$ 0.16	$ 0.08	$ 0.43
Diluted - pro forma	$ (0.16)	$ 0.15	$ (0.12)	$ 0.41
Risk free interest rate	3.60%	3.60%	3.60%	3.60%
Expected life of options	5 years	5 years	5 years	5 years
Expected volatility	40.9%	43.2%	40.9%	43.2%
Expected dividend yield				

The pro forma amounts may not be representative of future disclosures since the estimated fair value of stock options is amortized to expense over the vesting period and additional options may be granted in future years. Since changes in the subjective assumptions used in the Black-Scholes model can materially affect the fair value estimate, management believes the model does not provide a reliable measure of the fair value of its options.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 3 Stock Based Compensation (Continued)

On May 17 2005, the Compensation Committee of the Board of Directors of K2 approved the acceleration of vesting of certain unvested and out-of-the-money stock options previously awarded to employees and officers under the K2 stock option plans. An option was considered out-of-the-money if the stated exercise price was greater than $11.94 per share, the closing price of K2 s common stock on May 17, 2005, the last trading day before approval of the acceleration. Outstanding unvested options that had an exercise price equal to or less than $11.94 on May 17, 2005, will continue to vest under the terms of the original option agreements. As a result of this action, options to purchase approximately 2.1 million shares of K2 s common stock that would otherwise have vested over the next three years became fully vested on May 17, 2005. The affected options had a range of exercise prices of $12.51 to $14.30 and a weighted average exercise price of $13.14. Options held by non-employee directors were not affected. In addition, the Compensation Committee imposed a holding period that will require that all executive officers of the Company not sell shares acquired through the exercise of an accelerated option (other than shares needed to cover the exercise price and satisfying withholding taxes) prior to the earlier of the date on which exercise would have been permitted under the options original vesting terms or, if earlier, the executive officer s last day of employment.

The decision to accelerate the vesting of these options was made to reduce future compensation expense that is expected to be recorded in conjunction with K2 s adoption of SFAS 123 (Revised). The incremental expense associated with the acceleration of the options is included in the pro forma disclosures above for the three and six months ended June 30, 2005.

NOTE 4 Inventories

The components of inventories consisted of the following:

	June 30, 2005	December 31, 2004
	(Thousands)	
Finished goods	$ 271,473	$ 237,162
Work in process	15,934	15,389
Raw materials	79,720	72,574
	$ 367,127	$ 325,125

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

Note 5 Acquisitions

During the second quarter of 2005, K2 completed the acquisition of substantially all of the assets of Hodgman, Inc., a business engaged in the design, selling and distribution of hunting and fishing waders, and JRC Products Limited, a business engaged in the design, selling and distribution of fishing tackle products. The purchase prices for these acquisitions were paid in cash. The results of the operations of these two companies were included in the consolidated financial statements of K2 beginning with the respective dates of the acquisition.

The two transactions completed during the second quarter of 2005 were accounted for under the purchase method of accounting, and accordingly the purchased assets and liabilities were recorded at their estimated fair values at the respective date of acquisition. The combined preliminary purchase price allocation for the two acquisitions resulted in an excess of the aggregate purchase price over net tangible assets acquired of approximately $7.0 million.

Based on a preliminary independent third party valuation obtained during the second quarter of 2005, the excess amounts of the two transactions were preliminarily allocated to intangible assets with finite and indefinite lives including: customer relationships and patents of $0.1 million with an average life of two years; tradenames with an indefinite life not subject to amortization of $2.9 million; and goodwill not subject to amortization of $4.0 million.

The final allocations of the purchase price of these two transactions will be completed during the second half of 2005 based on K2 s final evaluation of such assets and liabilities.

At June 30, 2005, there was approximately $10.7 million of cash and 612,466 shares of K2 common stock held in escrow or due for payment relating to certain prior acquisitions. The cash and shares will be released from escrow during 2005 through 2008, subject to final agreement between K2 and the selling parties. The cash and shares in escrow, as well as future cash payments due have been reflected in the purchase price of the related acquisition. Shares held in escrow are reflected in the calculation of diluted earnings per share for the periods presented.

During 2004, K2 completed nine acquisitions, including the acquisitions of Fotoball (later renamed K2 Licensed Products, Inc.) on January 23, 2004, Ex Officio on May 12, 2004, Marmot on June 30, 2004 and Völkl and Marker on July 7, 2004, as well as five smaller acquisitions.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

Note 5 Acquisitions (Continued)

The consolidated condensed statements of income for the three and six months ended June 30, 2005 includes the operating results of each of the businesses acquired in 2004, however the consolidated condensed statements of income for the three and six months ended June 30, 2004 do not include the results of Marmot, Völkl and Marker or K2 s other acquisitions completed after the 2004 second quarter since these companies were acquired by K2 on or subsequent to June 30, 2004. The 2004 second quarter results include less than a full three months of results of Worr Game Products and IPI both of which were acquired by K2 on April 19, 2004, and Ex Officio, which was acquired by K2 on May 12, 2004. In addition, the 2004 six month results include less than a full six months of results of K2 Licensed Products which was acquired by K2 on January 23, 2004, Worr Game Products and IPI both of which were acquired by K2 on April 19, 2004, and Ex Officio, which was acquired by K2 on May 12, 2004.

The following summarized unaudited pro forma information of K2 assume the acquisitions of Marmot and Völkl and Marker had occurred as of January 1, 2004, the earliest date for which information is presented below. This pro forma information does not purport to be indicative of what would have occurred had the acquisitions been made as of those dates, or of results which may occur in the future. Pro forma results of operations of K2 s other acquisitions completed during 2004 and 2005 have not been presented because the effects of these additional acquisitions were not material on either an individual basis or aggregate basis to K2 s consolidated results of operations.

Pro Forma Information (Unaudited)
(Thousands, except per share amounts)

	For the three months ended June 30,		For the six months ended June 30,	
	2005	2004	2005	2004
Net sales	$ 301,425	$ 270,009	$ 619,716	$ 586,401
Operating income	8,346	1,899	18,357	16,534
Net income (loss)	1,453	(1,514)	3,777	4,762
Diluted earnings (loss) per share	$ 0.03	$ (0.04)	$ 0.08	$ 0.10

Pursuant to the acquisitions made by K2 during 2005, 2004 and 2003, K2 approved restructuring and exit plans related to the closure of certain facilities of the acquired companies. In accordance with Emerging Issues Task Force (EITF) 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination,* K2 established reserves for employee severance, employee relocation costs and lease termination costs totaling approximately $0.6 million, $11.0 million and $5.1 million, during 2005, 2004 and 2003 respectively. These reserves were recognized as assumed liabilities of the acquired companies. The reserves established were not individually significant to any of K2 s acquisitions during 2005, 2004 or 2003.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

Note 5-Acquisitions (Continued)

The following table summarizes the activity in 2004 and 2005:

	Employee Severance	Employee Relocation	Subtotal	Lease Termination Costs	Total
			(Thousands)		
Balance at December 31, 2003	$ 2,411	$ 816	$ 3,227	$ 1,203	$ 4,430
Reserves established in conjunction with acquisitions	6,968	40	7,008	4,034	11,042
Adjustments to reserve estimates (reflected as an adjustment of the cost of the acquired companies)	(974)		(974)		(974)
Utilized in 2004:	(1,415)	(488)	(1,903)	(40)	(1,943)
Balance at December 31, 2004	6,990	368	7,358	5,197	12,555
Reserves established in conjunction with acquisitions	253		253	370	623
Adjustments to reserve estimates (reflected as an adjustment of the cost of the acquired companies)	(634)		(634)		(634)
Utilized in 2005:	(1,668)	(121)	(1,789)	(219)	(2,008)
Balance at June 30, 2005	$ 4,941	$ 247	$ 5,188	$ 5,348	$ 10,536

K2 believes that the remaining reserves for restructuring are adequate to complete the restructuring and exit plans discussed above.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 6 Intangible Assets and Goodwill

The components of intangible assets and goodwill consisted of the following:

	Weighted Average Useful Life	June 30, 2005			December 31, 2004		
		Gross Amount	Accumulated Amortization	Net Book Value	Gross Amount	Accumulated Amortization	Net Book Value
				(Thousands)			
Intangibles subject to amortization:							
Patents	8.4 years	$ 15,575	$ 3,959	$ 11,616	$ 14,142	$ 3,161	$ 10,981
Customer contracts/relationships	8.2 years	8,215	2,101	6,114	8,139	1,488	6,651
Licensing agreements	5.2 years	2,795	1,113	1,682	2,795	868	1,927
Tradenames/trademarks	7.1 years	955	203	752	955	128	827
Non-compete agreements	3.9 years	1,572	444	1,128	1,347	212	1,135
Order backlog and other	0.2 years	1,430	1,430		1,040	1,285	(245)
		30,542	9,250	21,292	28,418	7,142	21,276
Intangibles not subject to amortization:							
(by segment)							
Tradename							
Marine and Outdoor		3,252		3,252	352		352
Team sports		39,287		39,287	33,687		33,687
Action sports		81,690		81,690	81,690		81,690
Apparel and Footwear		21,600		21,600	21,600		21,600
Goodwill							
Marine and Outdoor		26,720		26,720	22,853		22,853
Team sports		81,980		81,980	88,722		88,722
Action sports		152,485		152,485	156,211		156,211
Apparel and Footwear		81,903		81,903	81,974		81,974
		488,917		488,917	487,089		487,089
Total intangibles		$ 519,459	$ 9,250	$ 510,209	$ 515,507	$ 7,142	$ 508,365

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 6 Intangible Assets and Goodwill (Continued)

The table below shows the activity in intangibles subject to and not subject to amortization for the six months ended June 30, 2005, including the purchase price allocations completed by K2 during 2005 relating to the acquisitions completed by K2 in the second quarter of 2005 and fourth quarter of 2004, respectively. The preliminary and final purchase price allocations were based on independent third party valuations. The final allocations of the purchase price of the 2005 acquisitions will be completed by K2 during the second half of 2005.

	December 31, 2004				June 30, 2005
	Net Book Value	Purchase Price Allocations	Other Activity	Amortization	Net Book Value
Intangibles subject to amortization:					
Patents	$ 10,981	$ 430	$ 1,003	$ (798)	$ 11,616
Customer contracts/relationships	6,651	76		(613)	6,114
Licensing agreements	1,927			(245)	1,682
Tradenames/trademarks	827			(75)	752
Non-compete agreements	1,135	225		(232)	1,128
Order backlog and other	(245)	390		(145)	
	21,276	1,121	1,003	(2,108)	21,292
Intangibles not subject to amortization:					
(by segment)					
Tradename					
Marine and Outdoor	352	2,900			3,252
Team Sports	33,687	5,600			39,287
Action Sports	81,690				81,690
Apparel and Footwear	21,600				21,600
Goodwill					
Marine and Outdoor	22,853	3,973	(106)		26,720
Team Sports	88,722	(6,497)	(245)		81,980
Action Sports	156,211		(3,726)		152,485
Apparel and Footwear	81,974		(71)		81,903
	487,089	5,976	(4,148)		488,917
Total intangibles	$ 508,365	$ 7,097	$ (3,145)	$ (2,108)	$ 510,209

Amortization expense for intangibles subject to amortization was approximately $2.1 million for the six months ended June 30, 2005. Amortization expense of purchased intangible assets subject to amortization is estimated to be approximately $3.9 million during fiscal year ending 2005, $3.7 million during 2006, $3.5 million during 2007, $3.4 million during 2008 and $2.1 million during 2009.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 6 Intangible Assets and Goodwill (Continued)

Based on the results of the annual impairment tests, K2 determined that no impairment of goodwill or intangible assets with indefinite lives existed as of December 31, 2004 and no indicators of impairment were present during the six months ended June 30, 2005. However, future indicators or impairment tests of goodwill and intangible assets with indefinite lives could result in a charge to earnings. K2 will continue to evaluate goodwill and intangible assets with indefinite lives on an annual basis or whenever events and changes in circumstances indicate that there may be a potential impairment.

K2 has evaluated the remaining useful lives of its finite-lived purchased intangible assets to determine if any adjustments to the useful lives were necessary or if any of these assets had indefinite lives and were therefore not subject to amortization. K2 determined that no adjustments to the useful lives of its finite-lived purchased intangible assets were necessary.

K2 considered the recent softness in consumer demand for paintball products within its Action Sports segment and has determined that no indicators of impairment existed at June 30, 2005 with respect to certain indefinite and finite-lived intangibles. In the event consumer demand continues to remain soft for paintball products, K2 may be required to record an impairment charge in future periods related to indefinite and finite-lived intangibles within the Action Sports segment.

NOTE 7 Warranties

K2 records the estimated cost of product warranties at the time sales are recognized. K2 estimates warranty obligations by reference to historical product warranty return rates, material usage and service delivery costs incurred in correcting the product. Should actual product warranty return rates, material usage or service delivery costs differ from the historical rates, revisions to the estimated warranty liability would be required.

The following activity related to product warranty liabilities:

	Three Months Ended June 30		Six Months Ended June 30	
(Thousands)	**2005**	**2004**	**2005**	**2004**
Beginning Balance	$ 9,324	$ 5,520	$ 9,691	$ 5,526
Charged to costs and expenses	2,428	1,586	4,654	3,117
Increase to reserve resulting from acquisitions		325		325
Amounts charged to reserve	(2,379)	(966)	(4,972)	(2,503)

Ending Balance	$ 9,373	$ 6,465	$ 9,373	$ 6,465

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 8 Borrowings and Other Financial Instruments

At June 30, 2005, K2 s principal long-term borrowing facility was a five-year, $250.0 million revolving credit facility (the Facility) expiring on July 1, 2009 with several banks and other financial institutions. The Facility is expandable to $350.0 million subject to certain conditions. The Facility has a $100.0 million limit for the issuance of letters of credit. Borrowings under the Facility are secured by all of K2 s assets in the United States, Canada and England. Actual borrowing availability under the Facility is based on K2 s trade receivable and inventory levels in the United States, Canada and England, subject to eligibility criteria and defined advance rates. Borrowings under the Facility are subject to an interest rate grid, but as of June 30, 2005 bear a rate equal to the prime rate, or a LIBOR interest rate plus 2.00%, and the Facility had an unused commitment fee of 0.375% per year. The Facility includes various covenants, including requirements that K2 maintain a minimum debt service coverage ratio, as well as limiting annual capital expenditures, indebtedness, dividends and certain investment activities.

On March 18, 2005, K2 obtained an amendment to its Facility allowing K2 to make up to $50.0 million in repurchases of K2 common stock provided that unused borrowing availability under the facility is at least $50.0 million after such repurchases.

On July 25, 2005, K2 also obtained an amendment to its Facility allowing K2 to issue up to $100.0 million in unsecured notes, subject to the approval of the administrative agent, provided the issuance is completed within 365 days and the net proceeds are used to repay borrowings outstanding under the Facility.

At June 30, 2005, borrowings of $73.0 million were outstanding under the Facility bearing an average interest rate of 4.96%. At June 30, 2005, there were also letters of credit outstanding under the Facility of $20.5 million (consisting of $13.7 million of standby letters of credit and $6.8 million of trade letters of credit expiring over the next 12 months). K2 has classified $16.3 million of seasonal borrowings outstanding under the Facility at June 30, 2005 as current. Pursuant to the terms of the Facility, an additional $135.1 million was available for borrowing at June 30, 2005.

At June 30, 2005, K2 also had $25.0 million of 7.25% convertible subordinated debentures (7.25% Debentures) due March 2010 outstanding. The 7.25% Debentures are convertible into 2,097,315 shares of K2 common stock at a conversion price of $11.92 per share. Pursuant to the agreement for these debentures, the noteholders received warrants to purchase 243,260 and 524,329 additional shares of K2 s common stock at exercise prices of $13.14 and $11.92 per share, respectively, exercisable within the three and five year period ended February 14, 2006 and February 14, 2008, respectively (collectively, the Warrants). K2 assigned a total fair market value of $2,303,000 to the Warrants. At June 30, 2005, the aggregate unamortized fair market value of $1,231,000 is reflected as a reduction of the face amount of the 7.25% Debentures on K2 s balance sheet which is being amortized to interest expense using the effective interest method through the exercise periods, thereby increasing the carrying value of the debentures.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 8 Borrowings and Other Financial Instruments (Continued)

At June 30, 2005, K2 also had $75.0 million of 5.00% convertible senior debentures (5% Debentures) due June 2010 outstanding. The 5% Debentures are convertible into 5,706,458 shares of K2 common stock at a conversion price of $13.14 per share. The debentures are redeemable by K2 in whole or in part at K2 s option on or after June 15, 2008 at a redemption price of 101.429% beginning on June 15, 2008 and ending on June 14, 2009, and at 100.714% beginning on June 15, 2009 and ending on June 14, 2010.

At June 30, 2005, K2 also had $200.0 million of 7.375% senior, unsecured notes (Senior Notes) due July 1, 2014 outstanding. The Senior Notes are redeemable by K2 in whole or in part at K2 s option at any time prior to July 1, 2009 at a price equal to 100% of the principal amount plus accrued and unpaid interest plus a make-whole premium, as defined in the indenture. Thereafter, K2 may redeem all or a portion of the Senior Notes at the redemption prices set forth in the indenture. The Senior Notes include various incurrence covenants, including limitations on indebtedness, restricted payments and sales of assets.

At June 30, 2005, K2 also had $27.1 million outstanding under various foreign lending arrangements.

NOTE 9 Pension Plans

K2 sponsors several trusteed non-contributory defined benefit pension plans covering about 850 of its domestic employees. Benefits are generally based on years of service and the employee s highest average compensation for five consecutive years during the years of credited service. Contributions are intended to provide for benefits attributable to service to date and service expected to be provided in the future. K2 funds these plans in accordance with the Employee Retirement Income Security Act of 1974.

Effective August 31, 2004, the domestic pension plans (the plans) were amended to freeze the accrual of future benefits for almost all of the employees. This resulted in active participants no longer accruing benefits under the plans. Participants will remain eligible to receive benefits they have earned under the plans through August 31, 2004 when they retire. New employees will not be eligible to accrue any benefit under the plans. Only a small group of about 20 employees subject to a collective bargaining agreement will continue to accrue benefits. The impact of this change to the plans on K2 s benefit costs was a one-time recognized curtailment loss of $0.4 million in the 2004 third quarter. The impact on future benefit costs is the elimination of the service cost and an $8.0 million reduction of the projected benefit obligation for future pay increases. This change to the plans has further resulted in an estimated reduction in net periodic pension costs for the 2005 year of $2.8 million.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 9 Pension Plans (Continued)

The components of net periodic pension cost consisted of the following:

(Thousands)	For the three months ended June 30 2005	For the three months ended June 30 2004	For the six months ended June 30 2005	For the six months ended June 30 2004
Service cost	$ 25	$ 450	$ 50	$ 900
Interest cost	1,010	1,030	2,020	2,060
Expected return on assets	(1,034)	(910)	(2,068)	(1,820)
Amortization of:				
Prior service cost		15		30
Actuarial loss	162	135	324	270
Curtailment/settlement loss recognized				
Total net periodic benefit cost	$ 163	$ 720	$ 326	$ 1,440

The decline in the net periodic benefit cost for the three and six months ended June 30, 2005 as compared to the three and six months ended June 30, 2004 is due to K2 freezing its plans effective August 31, 2004. K2 s cash contribution to its plans in 2005 is expected to be $5.7 million. During the three and six months ended June 30, 2005, K2 made contributions totaling approximately $1.0 million and $1.5 million, respectively, to the plans.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 10 Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss are as follows:

	Currency Translation Adjustments	Additional Minimum Pension Liability	Derivative Financial Instruments	Total
		(Thousands)		
Balance at December 31, 2004	$ 7,143	$ (10,525)	$ (1,068)	$ (4,450)
Currency translation adjustment	(12,880)			(12,880)
Reclassification adjustment for amounts recognized in cost of sales			530	530
Change in fair value of derivatives, net of $290 in taxes			583	583
Balance at June 30, 2005	$ (5,737)	$ (10,525)	$ 45	$ (16,217)

Total comprehensive income (loss) was ($5.7) million and $6.5 million for the three months ended June 30, 2005 and 2004, respectively. Total comprehensive income (loss) was ($8.0) million and $17.3 million for the six months ended June 30, 2005 and 2004, respectively. Total comprehensive income (loss) includes the net change in accumulated other comprehensive loss for the period.

Adjustments resulting from translating foreign functional currency financial statements into U.S. dollars are included in the foreign currency translation adjustment in the above table. The currency translation loss for the six months ended June 30, 2005 is the result of the strengthening of the U.S. dollar against foreign currencies during the period, including the Euro, Japanese Yen and British Pound Sterling.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 11- Earnings Per Share Data

Basic earnings per share (EPS) is determined by dividing net income or loss by the weighted average number of shares outstanding during the period. Diluted EPS reflects the potential dilutive effects of stock options, restricted stock, common stock held in escrow and warrants, using the treasury stock method, and of the debentures using the if converted method. The table below provides a reconciliation from basic shares to fully diluted shares for the respective periods.

Options to purchase 4,450,291 and 3,588,884 shares of common stock were outstanding at June 30, 2005 and 2004, respectively. At June 30, 2005, there were also 230,000 unvested restricted stock awards outstanding and 612,466 shares held in escrow relating to certain acquisitions. At June 30, 2005 and 2004, $100.0 million of convertible debentures, convertible into 7,803,742 shares of common stock, and warrants to purchase 767,589 of shares of common stock were outstanding.

For the three months ended June 30, 2005 and 2004, approximately 2,167,000 and 424,000 stock options, respectively, were excluded since their inclusion would have been antidilutive. For the three months ended June 30, 2005 and 2004, 612,466 and 149,541 shares of common stock held in escrow, respectively, were included in the calculation of diluted EPS.

For the six months ended June 30, 2005 and 2004, approximately 1,500,000 and 435,000 stock options, respectively, were excluded since their inclusion would have been antidilutive. For the six months ended June 30, 2005 and 2004, 616,672 and 119,107 shares of common stock held in escrow, respectively, were included in the calculation of diluted EPS.

The EPS calculation for three and six months ended June 30, 2005 also excluded 7,803,742 shares from the issuance of the $100.0 million convertible subordinated debentures since their inclusion would have also been antidilutive.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 11- Earnings Per Share Data (Continued)

The table below outlines the determination of the number of diluted shares of common stock used in the calculation of diluted EPS as well as the calculation of diluted EPS for the periods presented:

	Three months ended June 30		Six months ended June 30	
	2005	2004	2005	2004
	(Thousands, except per share amounts)			
Determination of diluted number of shares:				
Average common shares outstanding	46,216	35,273	46,196	34,894
Assumed conversion of dilutive stock options and warrants	1,157	943	1,234	962
Assumed conversion of subordinated debentures		7,803		7,803
Diluted average common shares outstanding	47,373	44,019	47,430	43,659
Calculation of diluted earnings per share:				
Net income	$ 1,453	$ 6,178	$ 3,777	$ 16,918
Add: interest component on assumed conversion of subordinated debentures, net of taxes		918		1,836
Net income, adjusted	$ 1,453	$ 7,096	$ 3,777	$ 18,754
Diluted earnings per share (a)	$ 0.03	$ 0.16	$ 0.08	$ 0.43

(a) Diluted earnings per share is calculated by dividing net income, adjusted, by diluted average common shares outstanding for the respective period.

NOTE 12 Segment Information

As a result of recent acquisitions, beginning in the third quarter of 2004, K2 reclassified its business into the following four segments based on similar product types and distribution channels: Marine and Outdoor, Team Sports, Action Sports and Apparel and Footwear.

The Marine and Outdoor segment includes *Shakespeare* fishing tackle and monofilament products as well as *Stearns* outdoor products. The Team Sports segment includes baseball and softball products and *K2 Licensed Products.* The Action Sports segment includes skis, snowboards, snowshoes, in-line skates and paintball products. The Apparel and Footwear segment includes *Marmot* and *Ex Officio* products as well as skateboard shoes and related apparel.

The segment information for the 2004 period has been restated to reflect these reclassifications.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 12- Segment Information (Continued)

The segment information presented below is for the three months ended June 30:

	Net Sales to Unaffiliated Customers		Intersegment Sales		Operating Profit (Loss)	
	2005	2004 (a)	2005	2004 (a)	2005	2004 (a)
			(Millions)			
Marine and Outdoor	$ 130.4	$ 107.8	$ 36.8	$ 28.9	$ 20.1	$ 16.4
Team Sports	68.3	61.8			1.7	(0.7)
Action Sports	65.1	69.2	2.3		(10.7)	(1.0)
Apparel and Footwear	37.6	12.2	0.2	0.1	3.0	1.6
Total segment data	$ 301.4	$ 251.0	$ 39.3	$ 29.0	14.1	16.3
Corporate expenses, net					(4.6)	(3.7)
Interest expense					(7.3)	(3.2)
Income before provision for income taxes					$ 2.2	$ 9.4

(a) Results for the three months ended June 30, 2004 do not include the results of Völkl, Marker and Marmot or K2 s other acquisitions completed after the 2004 second quarter since these companies were acquired by K2 on or subsequent to June 30, 2004. In addition, the 2004 second quarter results include less than a full three months of results of Worr Game Products and IPI both of which were acquired by K2 on April 19, 2004, and Ex Officio, which was acquired by K2 on May 12, 2004.

The segment information presented below is for the six months ended June 30:

	Net Sales to Unaffiliated Customers		Intersegment Sales		Operating Profit (Loss)	
	2005	2004 (a)	2005	2004 (a)	2005	2004 (a)
			(Millions)			
Marine and Outdoor	$ 242.8	$ 206.6	$ 70.0	$ 49.3	$ 36.1	$ 31.7
Team Sports	160.9	155.9			10.6	10.3

Action Sports	145.5	144.2	5.0	0.0	(23.1)	(5.6)
Apparel and Footwear	70.5	21.7	1.0	0.4	3.9	2.1
Total segment data	$ 619.7	$ 528.4	$ 76.0	$ 49.7	27.5	38.5
Corporate expenses, net					(7.3)	(6.4)
Interest expense					(14.5)	(6.5)
Income before provision for income taxes					$ 5.7	$ 25.6

(a) Results for the six months ended June 30, 2004 do not include the results of Völkl, Marker and Marmot or K2 s other acquisitions completed after the 2004 second quarter since these companies were acquired by K2 on or subsequent to June 30, 2004. In addition, the 2004 six month results include less than a full six months of results of K2 Licensed Products which was acquired by K2 on January 23, 2004, Worr Game Products and IPI both of which were acquired by K2 on April 19, 2004, and Ex Officio, which was acquired by K2 on May 12, 2004.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 13 Contingencies

Certain of K2 s products are used in relatively high risk recreational settings and from time to time K2 is named as a defendant in lawsuits asserting product liability claims relating to its sporting goods products. To date, none of these lawsuits has had a material adverse effect on K2, and K2 does not expect any lawsuit now pending to have such an effect. K2 maintains product liability, general liability and excess liability insurance coverage. No assurances can be given such insurance will continue to be available at an acceptable cost to K2 or such coverage will be sufficient to cover one or more large claims, or that the insurers will not successfully disclaim coverage as to a pending or future claim.

K2 is one of several named potentially responsible parties (PRP) in three Environmental Protection Agency matters involving discharge of hazardous materials at old waste sites in South Carolina and Michigan. Although environmental laws technically impose joint and several liability upon each PRP at each site, the extent of K2 s required financial contribution to the clean-up of these sites is expected to be limited based upon the number and financial strength of the other named PRP s and the volume and types of waste involved which might be attributable to K2.

Environmental and related remediation costs are difficult to quantify for a number of reasons, including the number of parties involved, the difficulty in determining the extent of the contamination, the length of time remediation may require, the complexity of environmental regulation and the continuing advancement of remediation technology. K2 accrues for liabilities of this nature when it is probable a liability has been incurred and the amount can be reasonably estimated. At June 30, 2005 and December 31, 2004, K2 had recorded an estimated liability of approximately $800,000 for environmental liabilities. The estimate is based on K2 s share of the costs to remediate as provided by the PRP s consultants and in ongoing discussions with the EPA or other environmental agencies. The ultimate outcome of these matters cannot be predicted with certainty, however, and taking into consideration reserves provided, management does not believe these matters will have a material adverse effect on K2 s financial statements.

In January 2004, Rawlings was sued by a licensee in the U.S. District Court for the District of Maine in connection with a license agreement pursuant to which the licensee was granted an exclusive license to use certain Rawlings trademarks for the manufacture and sale of team and personal sporting-equipment bags. This lawsuit was later transferred to the U.S. District Court for the Eastern District of Missouri. In February 2004, Rawlings gave the licensee notice that it was terminating the license agreement and sued the licensee in the Missouri District Court, in which Rawlings alleged, among other things, that the licensee breached the license agreement by failing to use its best efforts. This license agreement was in place prior to the March 26, 2003 acquisition of Rawlings by K2 Inc. Accordingly, during 2004, K2 established liabilities totaling $3.5 million for the estimated probable settlement or verdict on the matter.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 13 Contingencies (Continued)

On April 29, 2005, a jury awarded the licensee (1) $4.1 million for a claim of lost profits for the next ten years on sales of equipment bags, plus the value of inventory of such bags (the 10-Year Lost Profits Verdict), (2) $2.1 million for lost profits of equipment bags beginning ten years from the date of the breach of the agreement through forever (the Speculative Profits Verdict) and (3) $2.5 million for K2 s alleged tortious interference with the licensee s business expectations (the Tortious Interference Verdict) between Rawlings and the licensee, and the Missouri District Court ruled that the licensee was not permitted to bring certain claims to the jury. Following trial, the licensee filed a motion to recover approximately $0.6 million in attorney s fees and costs this motion is currently pending. Following the verdict, K2 established an additional $1.2 million in liabilities for a total of approximately $4.7 million in liabilities related to this litigation, including estimated legal fees and costs of licensee s attorneys.

On May 19, 2005, K2 and Rawlings, (the Litigants), filed a motion for new trial with respect to the 10-Year Lost Profits Verdict and a motion for judgment notwithstanding the verdict with respect to the Speculative Profits Verdict and the Tortious Interference Verdict. On July 27, 2005, the Missouri District (1) denied the Litigants motion for a new trial in respect of the $4.1 million 10-Year Lost Profits Verdict, (2) granted the Litigants motion for judgment notwithstanding the verdict with respect to the $2.1 million Speculative Profits Verdict and (3) denied the Litigants motion for judgment notwithstanding the verdict for the $2.5 million Tortious Interference Verdict. The only matter that remains open for the Missouri District Court is the licensee s motion for approximately $0.6 million in attorneys fees and costs. Accordingly, there is currently a judgment against the Litigants for approximately $6.8 million.

The Litigants intend to vigorously prosecute an appeal. K2 believes, in part based on advice and estimates from outside counsel as follows: that certain portions of the Missouri District Court s decision are not supported by facts or law; that there are meritorious arguments to be raised during the appeals process because, among other things, a lack of evidence to support certain aspects of the verdict; and that the Litigants aggregate exposure, including attorney s fees and costs of license, to be approximately $4.7 million. In connection with the appeal, the Litigants will be required by Missouri law to post bond in the amount of approximately $6.8 million. In the event that the Litigants are unsuccessful in their appeal and the amount of the judgment, including the fees and costs of attorneys for licensee, is greater than $4.7 million, or the outcome of an amount greater than $4.7 million becomes probable and estimable, K2 will be required to record an expense in the period in which the matter is finalized. However, this expense could be higher if the appeals court ruled in favor of the licensee for certain claims on which it is expected that licensee will appeal. The appeal process is expected to take one to two years.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 13 Contingencies (Continued)

K2 is involved in lawsuits, claims, investigations and proceedings, including those identified above, consisting of product liability, patent, commercial, employment and environmental matters, which arise in the ordinary course of business. In accordance with SFAS No. 5, *Accounting for Contingencies*, K2 makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. K2 believes that it has adequate provisions for such matters. K2 reviews these provisions at least quarterly and adjusts these provisions to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular legal matter. Litigation is inherently unpredictable. However, K2 believes that it has valid defenses with respect to legal matters pending against it. Nevertheless, it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of one or more of these contingencies.

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 14 Supplemental Guarantor Information

Obligations to pay principal and interest on K2 s Senior Notes are guaranteed fully and unconditionally by K2 s existing and future wholly-owned U.S. subsidiaries. Separate financial statements of the guarantors are not provided, as subsidiary guarantors are 100% owned by K2 and guarantees are full, unconditional and joint and several. The non-guarantor subsidiaries are K2 s consolidated non-U.S. subsidiaries. Supplemental condensed consolidating financial information of the K2 s guarantors is presented below.

Condensed Consolidating Statements of Income (Unaudited)

(Thousands)

	For the three months ended June 30, 2005				
	K2 Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminating Entries	Consolidated K2 Inc.
			(Thousands)		
Net sales	$	$ 243,765	$ 96,935	$ (39,275)	$ 301,425
Cost of products sold		164,830	74,557	(37,720)	201,667
Gross profit		78,935	22,378	(1,555)	99,758
Selling expenses	542	38,233	15,727		54,502
General and administrative expenses	8,161	20,467	8,282		36,910
Operating income (loss)	(8,703)	20,235	(1,631)	(1,555)	8,346
Other income, net	(15)	(878)	(224)		(1,117)
Interest expense	5,695	49	1,541		7,285
Income (loss) before income taxes	(14,383)	21,064	(2,948)	(1,555)	2,178
Income taxes		1,411	(686)		725
Net income (loss)	$ (14,383)	$ 19,653	$ (2,262)	$ (1,555)	$ 1,453

	For the three months ended June 30, 2004				
	K2 Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminating Entries	Consolidated K2 Inc.
Net sales	$	$ 196,134	$ 83,847	$ (28,994)	$ 250,987
Cost of products sold	(1,403)	136,480	67,558	(29,013)	173,622

Gross profit	1,403	59,654	16,289	19	77,365
Selling expenses	423	28,810	12,372	(39)	41,566
General and administrative expenses	5,330	15,345	5,046	(2,367)	23,354
Operating income (loss)	(4,350)	15,499	(1,129)	2,425	12,445
Other income, net	(2)	(2,494)	(359)	2,730	(125)
Interest expense	3,105	(24)	130	(1)	3,210
Income (loss) before income taxes	(7,453)	18,017	(900)	(304)	9,360
Income taxes		3,875	(693)		3,182
Net income (loss)	$ (7,453)	$ 14,142	$ (207)	$ (304)	$ 6,178

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 14 Supplemental Guarantor Information (Continued)

Condensed Consolidating Statements of Income - Continued (Unaudited)

(Thousands)

	For the six months ended June 30, 2005				
	K2 Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminating Entries	Consolidated K2 Inc.
Net sales	$	$ 492,659	$ 202,997	$ (75,940)	$ 619,716
Cost of products sold		334,119	155,939	(72,919)	417,139
Gross profit		158,540	47,058	(3,021)	202,577
Selling expenses	1,097	79,514	32,606		113,217
General and administrative expenses	15,121	40,700	15,182		71,003
Operating income (loss)	(16,218)	38,326	(730)	(3,021)	18,357
Other income, net	(821)	(677)	(340)		(1,838)
Interest expense	12,441	202	1,895		14,538
Income (loss) before income taxes	(27,838)	38,801	(2,285)	(3,021)	5,657
Income taxes		2,451	(571)		1,880
Net income (loss)	$ (27,838)	$ 36,350	$ (1,714)	$ (3,021)	$ 3,777

	For the six months ended June 30, 2004				
	K2 Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminating Entries	Consolidated K2 Inc.
Net sales	$	$ 429,246	$ 148,832	$ (49,727)	$ 528,351
Cost of products sold		296,184	117,907	(49,738)	364,353
Gross profit		133,062	30,925	11	163,998
Selling expenses	603	65,147	17,952	(89)	83,613
General and administrative expenses	10,399	32,767	7,619	(2,367)	48,418
Operating income (loss)	(11,002)	35,148	5,354	2,467	31,967
Other income, net		(2,602)	(316)	2,740	(178)
Interest expense	6,287	83	143	(1)	6,512

Income (loss) before income taxes	(17,289)	37,667	5,527	(272)	25,633
Income taxes		7,223	1,492		8,715
Net income (loss)	$ (17,289)	$ 30,444	$ 4,035	$ (272)	$ 16,918

K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 14 Supplemental Guarantor Information (Continued)

Condensed Consolidating Balance Sheets (Unaudited)

(Thousands)

	As of June 30, 2005				
	K2 Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminating Entries	Consolidated K2 Inc.
Assets					
Current Assets					
Cash and cash equivalents	$ 4,835	$ 409	$ 16,206	$	$ 21,450
Accounts receivable, net	36,522	235,432	116,343	(123,453)	264,844
Inventories, net	36	242,549	129,863	(5,321)	367,127
Deferred income taxes	32,640			(11,772)	20,868
Prepaid expenses and other current assets	565	6,893	20,693		28,151
Total current assets	74,598	485,283	283,105	(140,546)	702,440
Property, plant and equipment	12,455	159,655	112,079		284,189
Less allowance for depreciation and amortization	994	99,717	42,143		142,854
	11,461	59,938	69,936		141,335
Intangible assets, net	429,637	14,745	65,827		510,209
Deferred income taxes	7,506				7,506
Investment in subsidiaries	680,285			(680,285)	
Other	19,888	2,917	1,572		24,377
Total Assets	$ 1,223,375	$ 562,883	$ 420,440	$ (820,831)	$ 1,385,867
Liabilities and Shareholders Equity					
Current Liabilities					
Bank loans	$	$	$ 7,017	$	$ 7,017
Accounts payable	431	99,077	72,707	(98,611)	73,604
Accrued liabilities	67,481	60,879	41,843		170,203
Current portion of long-term debt	16,293		2,830		19,123
Total current liabilities	84,205	159,956	124,397	(98,611)	269,947
Long-term pension liabilities	16,854				16,854
Long-term debt	256,707		17,297		274,004
Deferred income taxes	47,764	7,343	7,411	(11,772)	50,746
Advances (to) from affiliates. net	43,529	(63,802)	50,436	(30,163)	
Convertible subordinated debentures	98,769				98,769

Interdivisional equity		459,386	220,899	(680,285)	
Shareholders Equity	675,547				675,547
Total Liabilities and Shareholders Equity	$ 1,223,375	$ 562,883	$ 420,440	$ (820,831)	$ 1,385,867

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K2 INC.

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

June 30, 2005

NOTE 14 Supplemental Guarantor Information (Continued)

Condensed Consolidating Balance Sheets

(Thousands)

	As of December 31, 2004				
	K2 Inc.	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminating Entries	Consolidated K2 Inc.
Assets					
Current Assets					
Cash and cash equivalents	$ 3,167	$ 5,098	$ 17,368	$	$ 25,633
Accounts receivable, net	54,123	240,539	176,633	(101,381)	369,914
Inventories, net	1,479	214,336	115,337	(6,027)	325,125
Deferred income taxes	27,970	14	1,725		29,709
Prepaid expenses and other current assets	716	5,582	16,477		22,775
Total current assets	87,455	465,569	327,540	(107,408)	773,156
Property, plant and equipment	8,548	153,883	110,528		272,959
Less allowance for depreciation and amortization	638	93,939	37,418		131,995
	7,910	59,944	73,110		140,964
Investment in affiliates	560,820			(560,820)	
Intangible assets, net	484,109	13,431	5,825	5,000	508,365
Deferred income taxes	7,506				7,506
Other	20,707	2,702	2,965		26,374
Total Assets	$ 1,168,507	$ 541,646	$ 409,440	$ (663,228)	$ 1,456,365
Liabilities and Shareholders Equity					
Current Liabilities					
Bank loans	$	$	$ 31,490	$	$ 31,490
Accounts payable	3,054	95,462	84,369	(79,727)	103,158
Accrued liabilities	59,993	58,520	60,940		179,453
Current portion of long-term debt	30,455	421	4,198		35,074
Total current liabilities	93,502	154,403	180,997	(79,727)	349,175
Long-term pension liabilities	16,854				16,854
Long-term debt	229,736	1,624	19,452		250,812
Deferred income taxes	52,048	6,075			58,123
Advances (to) from affiliates, net	(5,034)	(32,645)	60,360	(22,681)	
Convertible subordinated debentures	98,535				98,535

Interdivisional equity		412,189	148,631	(560,820)	
Shareholders Equity	682,866				682,866