

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

NL INDUSTRIES INC
Form 10-Q/A
December 23, 2005

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A
(Amendment No. 1)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934

For the quarter ended June 30, 2005 Commission file number 1-640

NL INDUSTRIES, INC.

(Exact name of Registrant as specified in its charter)

New Jersey

13-5267260

(State or other jurisdiction of
incorporation or organization)

(IRS Employer
Identification No.)

5430 LBJ Freeway, Suite 1700, Dallas, Texas 75240-2697

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (972) 233-1700

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 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 Securities Exchange Act of 1934). Yes X No
--- ---

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Number of shares of the Registrant's common stock outstanding on July 29, 2005: 48,556,134.

Explanatory Note Regarding Amendment No. 1

The Registrant hereby files this Report on Form 10-Q/A ("Form 10-Q/A") to amend its Quarterly Report on Form 10-Q for the quarter ended June 30, 2005, as filed with the Securities and Exchange Commission ("SEC") on August 3, 2005 ("Original Form 10-Q"). As discussed in Note 1 to the Consolidated Financial Statements, on December 21, 2005, the Registrant and its audit committee concluded that the Registrant would file this Form 10-Q/A to restate the Registrant's consolidated balance sheet as of December 31, 2004 and June 30, 2005, and the Registrant's consolidated statements of income, comprehensive income, cash flows and stockholders' equity for the interim periods ended June 30, 2004 and 2005, in each case as contained in the Original Form 10-Q.

As previously disclosed, prior to December 2003 Kronos Worldwide, Inc. was a wholly-owned subsidiary of the Company. In December 2003, the Registrant completed the distribution of approximately 48.8% of Kronos' common stock on a pro-rata basis to its shareholders, and during 2004 the Registrant paid each of its four \$.20 per share regular quarterly dividends in the form of shares of Kronos common stock. Consequently, effective in July 2004 the Registrant's ownership of Kronos was reduced to less than 50%, and the Registrant commenced to account for its interest in Kronos by the equity method.

The Registrant is a majority-owned subsidiary of Valhi, Inc., and majority ownership of Kronos continues to reside with Valhi and its subsidiaries, including the Registrant. Valhi is a majority-owned subsidiary of Contran Corporation. The Registrant and Valhi are members of the Contran Tax Group, and the Registrant computes its provision for income taxes on a separate company basis.

In its previously-issued consolidated financial statements, the Registrant accounted for any current income tax resulting from the distribution of shares of Kronos common stock to its shareholders as a direct charge to equity. In addition, the Registrant commenced to recognize deferred income taxes with respect to the excess of the financial reporting carrying value of its investment in Kronos over the adjusted income tax basis of such shares starting in July 2004, concurrent with the Registrant beginning to account for its interest in Kronos by the equity method, on a prospective basis. The Registrant has now concluded, among other things, that (i) a portion of the current income taxes resulting from the distribution of shares of Kronos common stock to its shareholders should be included in the Registrant's provision for income taxes included in the determination of net income and (ii) the Registrant should have commenced to recognize deferred income taxes with respect to the excess of the financial reporting carrying value of its investment in Kronos over the adjusted income tax basis of such shares starting with such excess that existed in December 2003, concurrent with its distribution of 48.8% of Kronos' common stock in December 2003.

Accordingly, during the Registrant's close process for its fiscal quarter ended September 30, 2005, the Registrant concluded that:

- o its provision for income taxes included in the determination of income from continuing operations was misstated by an aggregate of \$43.3 million, or \$.89 per diluted share, in the second quarter of 2004, by \$42.9 million, or \$.88 per diluted share, in the first six months of 2004, by \$81,000, or nil

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

- per share, in the second quarter of 2005 and by \$1.2 million, or \$.04 per diluted share, in the first six months of 2005;
- o its provision for deferred income taxes included in the determination of total other comprehensive income related to foreign currency translation was misstated by an aggregate of \$1.0 million in the six months of 2004 and by \$8,000 in the first six months of 2005;
 - o its provision for income taxes accounted for as a direct reduction to stockholders' equity was misstated by \$913,000 in the first quarter of 2005; and
 - o with respect to its statement of changes in stockholders' equity, and in addition to the effect of the items noted above, total stockholders' equity was misstated by \$58.1 million as of December 31, 2004,

in each case as they related to the appropriate provision for income taxes and related items (including a \$174.5 million increase to stockholders' equity in 2004 resulting from the settlement of a \$227 million income tax liability by using 5.5 million shares of Kronos common stock with an aggregate \$52.5 million carrying amount) which should have been recognized in accordance with accounting principles generally accepted in the United States of America ("GAAP") as provided by the guidance contained in Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes, with respect to the following items:

- o Deferred income taxes with respect to the income tax effect of the excess of the GAAP book basis over the income tax basis of the Registrant's investment in Kronos Worldwide, Inc., which investment the Registrant accounts for by the equity method, giving consideration to NL's investment in Kronos on a pure stand-alone separate company basis without regard to tax group membership with other affiliated companies;
- o Current and deferred income taxes related to the Registrant's distributions or transfer of shares of Kronos common stock to its stockholders (including entities under common control); and
- o Current and deferred income tax provisions related to other items.

In addition to the above items, the Company has also recognized another immaterial restatement item with respect to the Company's consolidated balance sheet at June 30, 2005.

This amendment was required to correct for the aggregate effect of these misstatements. See Note 1 to the Consolidated Financial Statements for a summary of financial statement amounts that are affected by this restatement. While the effect of these misstatements have no effect on the Registrant's previously-reported total cash flows from operating, investing and financing activities, these misstatements do have a significant effect on the Registrant's provision for income taxes, related income tax accounts (principally deferred income taxes) and stockholders' equity.

The guidance set forth in Auditing Standards No. 2 of the Public Company Accounting Oversight Board states that a restatement of previously-issued financial statements to reflect the correction of a misstatement should be regarded as at least a significant control deficiency and as a strong indicator that a material weakness in internal control over financial reporting exists. As a result of this amendment, the Registrant has concluded that a material weakness existed at June 30, 2005 that precludes the Registrant from concluding that its internal control over financial reporting was effective as of such date. Therefore, the Company's previous conclusion that it maintained effective internal control over financial reporting as of June 30, 2005, as set forth in the Original Form 10-Q, has been restated. See Item 4 - "Controls and Procedures."

For the convenience of the reader, this Form 10-Q/A sets forth the Original Form 10-Q, as amended hereby, in its entirety. However, this Form 10-Q/A only amends and restates Items 1, 2 and 4 of the Original Form 10-Q, in each case

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

solely as a result of and to reflect the corrections discussed above, and no other information in the Original Form 10-Q is amended hereby. The foregoing items have not been updated to reflect other events occurring after the filing of the Original Form 10-Q, or to modify or update those disclosures affected by other subsequent events. In addition, pursuant to the rules of the SEC, Exhibits 31.1, 31.2 and 32.1 have been updated to contain currently-dated certifications of the Registrant's Chief Executive Officer and Chief Financial Officer.

NL INDUSTRIES, INC. AND SUBSIDIARIES

INDEX

	Page number	
Part I.	FINANCIAL INFORMATION	
Item 1.	Financial Statements	
	Consolidated Balance Sheets - December 31, 2004 (Restated); June 30, 2005 (Unaudited and Restated)	5
	Consolidated Statements of Income - Three months and six months ended June 30, 2004 (Unaudited and Restated); Three months and six months ended June 30, 2005 (Unaudited and Restated)	7
	Consolidated Statements of Comprehensive Income - Six months ended June 30, 2004 (Unaudited and Restated); Six months ended June 30, 2005 (Unaudited and Restated)	8
	Consolidated Statement of Stockholders' Equity - Six months ended June 30, 2005 (Unaudited and Restated)	9
	Consolidated Statements of Cash Flows - Six months ended June 30, 2004 (Unaudited and Restated); Six months ended June 30, 2005 (Unaudited and Restated)	10
	Notes to Consolidated Financial Statements (Unaudited)	12
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	28
Item 4.	Controls and Procedures	42
Part II.	OTHER INFORMATION	
Item 1.	Legal Proceedings	44
Item 4.	Submission of Matters to a Vote of Security Holders	44
Item 6.	Exhibits	44

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands)

ASSETS	December 31, 2004 ----- (Restated)	June 30, 2005 ----- (Unaudited) (Restated)
Current assets:		
Cash and cash equivalents	\$ 99,185	\$ 101,190
Restricted cash and cash equivalents	7,810	4,691
Restricted marketable debt securities	9,446	11,538
Accounts and other receivables	24,302	23,323
Refundable income taxes	32	644
Receivable from affiliates	1,681	422
Inventories	28,781	19,945
Prepaid expenses	1,332	2,284
Deferred income taxes	13,604	5,478
	-----	-----
Total current assets	186,173	169,515
	-----	-----
Other assets:		
Marketable equity securities	75,793	82,437
Restricted marketable debt securities	3,848	-
Investment in Kronos Worldwide, Inc.	175,578	180,928
Receivable from affiliate	10,000	8,000
Deferred income taxes	545	-
Goodwill	20,772	21,020
Other	3,715	7,505
	-----	-----
Total other assets	290,251	299,890
	-----	-----
Property and equipment:		
Land	5,356	8,787
Buildings	26,877	26,977
Equipment	127,044	104,419
Construction in progress	2,431	5,172
	-----	-----
	161,708	145,355
Less accumulated depreciation and amortization	86,490	76,511
	-----	-----
Net property and equipment	75,218	68,844
	-----	-----
	\$ 551,642	\$ 538,249
	=====	=====

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

See accompanying notes to consolidated financial statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (CONTINUED)
(In thousands)

LIABILITIES AND STOCKHOLDERS' EQUITY	December 31, 2004	June 30, 2005
	----- (Restated)	----- (Unaudited) (Restated)
Current liabilities:		
Current maturities of long-term debt	\$ 42	\$ 41
Accounts payable	14,649	12,498
Accrued liabilities	23,134	29,920
Accrued environmental costs	16,570	16,688
Payable to affiliates	391	3,366
Income taxes	3,661	852
Deferred income taxes	23,842	-
	-----	-----
Total current liabilities	82,289	63,365
	-----	-----
Noncurrent liabilities:		
Long-term debt	85	64
Accrued pension costs	7,968	7,155
Accrued postretirement benefits costs	10,572	9,939
Accrued environmental costs	51,247	48,128
Deferred income taxes	103,420	108,563
Other	4,028	3,102
	-----	-----
Total noncurrent liabilities	177,320	176,951
	-----	-----
Minority interest	58,404	49,274
	-----	-----
Stockholders' equity:		
Common stock	6,054	6,069
Additional paid-in capital	369,728	372,339
Retained earnings	-	6,575
Accumulated other comprehensive income (loss):		
Marketable securities	26,783	31,012

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Currency translation	(135,729)	(134,129)
Pension liabilities	(33,207)	(33,207)
	-----	-----
Total stockholders' equity	233,629	248,659
	-----	-----
	\$ 551,642	\$ 538,249
	=====	=====

Commitments and contingencies (Notes 12 and 14)

See accompanying notes to consolidated financial statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)
(Unaudited)

	Three months ended June 30,	
	2004 (Restated)	2005 (Restated)
Net sales	\$ 342,036	\$ 45,730
Cost of sales	262,837	35,203
	-----	-----
Gross margin	79,199	10,527
Selling, general and administrative expense	41,096	5,808
Other operating income (expense):		
Currency transaction gains (losses), net	471	39
Disposition of property and equipment	21	-
Other income	6,858	1,178
Corporate expense	(4,584)	(4,223)
	-----	-----
Income from operations	40,869	1,713
Equity in earnings of Kronos Worldwide, Inc.	-	11,766
Other income (expense):		
Trade interest income	273	23
Interest and dividend income from affiliates	815	620
Other interest income	352	794

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Securities transactions, net	(3)	118
Interest expense	(8,741)	(117)
	-----	-----
Income from continuing operations before income taxes and minority interest	33,565	14,917
Provision (benefit) for income taxes	(255,369)	4,247
Minority interest in after-tax earnings	142,543	785
	-----	-----
Income from continuing operations	146,391	9,885
Discontinued operations	185	-
	-----	-----
Net income	\$ 146,576	\$ 9,885
	=====	=====
Cash dividend per share	\$ -	\$.25
	=====	=====
Earnings per share:		
Basic net income per share	\$ 3.03	\$.20
	=====	=====
Diluted net income per share	\$ 3.03	\$.20
	=====	=====
Weighted-average shares used in the calculation of net income per share:		
Basic	48,361	48,553
Dilutive impact of stock options	63	40
	-----	-----
	48,424	48,593
	=====	=====

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Six months ended June 30, 2004 and 2005

(In thousands)

(Unaudited)

	2004	2005
	-----	-----
	(Restated)	(Restated)
Net income	\$ 152,073	\$ 24,375

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Other comprehensive income (loss), net of tax:		
Marketable securities adjustment -		
unrealized holding gains (losses) arising		
during the period	(11,082)	4,229
Currency translation adjustment, net of tax	(2,978)	1,600
	-----	-----
Total other comprehensive income (loss)	(14,060)	5,829
	-----	-----
Comprehensive income	\$ 138,013	\$ 30,204
	=====	=====

See accompanying notes to consolidated financial statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

Six months ended June 30, 2005

(In thousands)

(Unaudited)

	Common stock	Additional paid-in capital	Retained earnings	Marketable securities	Accumulat comprehensive Curre transla
	-----	-----	-----	-----	-----
		(Restated)	(Restated)		(Resta
Balance at December 31, 2004:					
Previously reported	\$6,054	\$417,760	\$ 10,970	\$ 26,783	\$ (136,
Prior period adjustments	-	(48,032)	(10,970)	-	-----
	-----	-----	-----	-----	-----
Balance, as restated	6,054	369,728	-	26,783	(135,
Net income (Restated)	-	-	24,375	-	-
Issuance of common stock	15	2,490	-	-	-
Dividends	-	-	(12,139)	-	-

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Distribution of shares of Kronos Worldwide, Inc. common stock	-	-	(2,637)	-	-
Income tax on distribution	-	-	(3,024)	-	-
Other comprehensive income, net (Restated)	-	-	-	4,229	1,
Other	-	121	-	-	-
	-----	-----	-----	-----	-----
Balance at June 30, 2005 (Restated)	\$6,069	\$372,339	\$ 6,575	\$ 31,012	\$ (134,
	=====	=====	=====	=====	=====

See accompanying notes to consolidated financial statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

Six months ended June 30, 2004 and 2005

(In thousands)

(Unaudited)

	2004	2005
	-----	-----
	(Restated)	(Restated)
Cash flows from operating activities:		
Net income	\$ 152,073	\$ 24,375
Depreciation and amortization	29,289	5,567
Deferred income taxes:		
Continuing operations	(263,766)	(14,683)
Discontinued operations	94	(187)
Minority interest:		
Continuing operations	147,919	1,515
Discontinued operations	(94)	(151)
Equity in earnings of Kronos Worldwide, Inc.	-	(19,556)
Distributions from Kronos Worldwide, Inc.	-	8,835
Distributions from TiO2 manufacturing joint venture	8,300	-
Net (gains) losses from securities transactions	25	(14,696)
Other, net	1,526	(142)
Change in assets and liabilities:		
Accounts and other receivables	(52,976)	(3,542)
Inventories	52,614	756
Prepaid expenses	933	(603)
Accrued environmental costs	(4,932)	(2,918)
Accounts payable and accrued liabilities	(26,407)	(490)
Income taxes	27,492	(6,837)
Accounts with affiliates	693	3,777

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Other, net	(1,166)	867
	-----	-----
Net cash provided (used) by operating activities	71,617	(18,113)
	-----	-----
Cash flows from investing activities:		
Capital expenditures	(12,660)	(7,394)
Collection of loans to affiliates	2,000	2,000
Change in restricted cash equivalents and marketable debt securities, net	2,470	3,118
Proceeds from disposal of:		
Business unit	-	18,094
Kronos common stock	-	19,176
Property and equipment	2,119	12
Cash of disposed business unit	-	(4,006)
Purchase of shares of CompX International Inc.	-	(572)
Other, net	84	-
	-----	-----
Net cash provided (used) by investing activities	(5,987)	30,428
	-----	-----

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)

Six months ended June 30, 2004 and 2005

(In thousands)

(Unaudited)

	2004	2005
	-----	-----
	(Restated)	(Restated)
Cash flows from financing activities:		
Indebtedness:		
Borrowings	\$ 102,220	\$ -
Principal payments	(126,072)	(19)
Deferred financing costs paid	(28)	(28)
Dividends paid	-	(12,139)
Distributions to minority interest	(12,036)	(1,203)
Proceeds from issuance of common stock:		
NL common stock	8,286	2,693
CompX common stock	330	217
	-----	-----
Net cash used by financing activities	(27,300)	(10,479)
	-----	-----
Cash and cash equivalents - net change from:		

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Operating, investing and financing activities	38,330	1,836
Currency translation	(481)	169
Cash and cash equivalents at beginning of period	89,525	99,185
	-----	-----
Cash and cash equivalents at end of period	\$ 127,374	\$ 101,190
	=====	=====
 Supplemental disclosures:		
Cash paid (received) for:		
Interest, net of amounts capitalized	\$ 17,119	\$ 82
Income taxes, net	(20,126)	27,764
 Noncash investing activity - note receivable received upon disposal of business unit		
	\$ -	\$ 4,179

See accompanying notes to consolidated financial statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1 - Restatements, organization and basis of presentation and other:

Restatement of financial statements

On December 21, 2005, the Company and its audit committee concluded that the Company would file this Quarterly Report on Form 10-Q/A for the quarter ended June 30, 2005 to restate the Company's consolidated balance sheet as of December 31, 2004 and June 30, 2005, and the Company's consolidated statements of income, comprehensive income, cash flows and stockholders' equity for the interim periods ended June 30, 2004 and 2005.

As discussed below in Notes 1 and 2, prior to December 2003 Kronos Worldwide, Inc. was a wholly-owned subsidiary of the Company. In December 2003, NL completed the distribution of approximately 48.8% of Kronos' common stock on a pro-rata basis to its shareholders, and during 2004 NL paid each of its four \$.20 per share regular quarterly dividends in the form of shares of Kronos common stock. Consequently, effective in July 2004 the Company's ownership of Kronos was reduced to less than 50%, and the Company commenced to account for its interest in Kronos by the equity method.

The Company is a majority-owned subsidiary of Valhi, Inc., and majority ownership of Kronos continues to reside with Valhi and its subsidiaries, including the Company. Valhi is a majority-owned subsidiary of Contran Corporation. The Company and Valhi are members of the Contran Tax Group, and the Company computes its provision for income taxes on a separate company basis.

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

In its previously-issued consolidated financial statements, the Company accounted for any current income tax resulting from the distribution of shares of Kronos common stock to its shareholders as a direct charge to equity. In addition, the Company commenced to recognize deferred income taxes with respect to the excess of the financial reporting carrying value of its investment in Kronos over the adjusted income tax basis of such shares starting in July 2004, concurrent with the Company beginning to account for its interest in Kronos by the equity method, on a prospective basis. The Company has now concluded, among other things, that (i) a portion of the current income taxes resulting from the distribution of shares of Kronos common stock to its shareholders should be included in the Company's provision for income taxes included in the determination of net income and (ii) the Company should have commenced to recognize deferred income taxes with respect to the excess of the financial reporting carrying value of its investment in Kronos over the adjusted income tax basis of such shares starting with such excess that existed in December 2003, concurrent with its distribution of 48.8% of Kronos' common stock in December 2003.

During the Company's close process for its fiscal quarter ended September 30, 2005, the Company concluded that:

- o its provision for income taxes included in the determination of income from continuing operations was misstated by an aggregate of \$43.3 million, or \$.89 per diluted share, in the second quarter of 2004, by \$42.9 million, or \$.88 per diluted share, in the first six months of 2004, by \$81,000, or nil per share, in the second quarter of 2005 and by \$1.2 million, or \$.04 per diluted share, in the first six months of 2005;
- o its provision for deferred income taxes included in the determination of total other comprehensive income related to foreign currency translation was misstated by an aggregate of \$1.0 million in the six months of 2004 and by \$8,000 in the first six months of 2005;
- o its provision for income taxes accounted for as a direct reduction to stockholders' equity was misstated by \$913,000 in the first six months of 2005; and
- o with respect to its statement of changes in stockholders' equity and in addition to the effect of the items noted above, total stockholders' equity was misstated by \$58.1 million as of December 31, 2004,

in each case as they related to the appropriate provision for income taxes and related items (including a \$174.5 million increase to stockholders' equity in 2004 resulting from the settlement of a \$227 million income tax liability by using 5.5 million shares of Kronos common stock with an aggregate \$52.5 million carrying amount) which should have been recognized in accordance with accounting principles generally accepted in the United States of America ("GAAP") as provided by the guidance contained in Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes, with respect to the following items:

- o Deferred income taxes with respect to the income tax effect of the excess of the GAAP book basis over the income tax basis of the Registrant's investment in Kronos Worldwide, Inc., which investment the Registrant accounts for by the equity method, giving consideration to NL's investment in Kronos on a pure stand-alone separate company basis without regard to tax group membership with other affiliated companies;
- o Current and deferred income taxes related to the Registrant's distributions or transfer of shares of Kronos common stock to its stockholders (including entities under common control); and
- o Current and deferred income tax provisions related to other items.

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

On December 21, 2005, the Company and its audit committee concluded that the Company had failed to properly apply the guidance contained in SFAS No. 109 in so far as it related to these items. This amendment was required to correct for the aggregate effect of these misstatements. While the effect of these misstatements have no effect on the Company's previously-reported total cash flows from operating, investing and financing activities, these misstatements do have a significant effect on the Company's provision for income taxes, related income tax accounts (principally deferred income taxes) and stockholders' equity.

In addition to the above items, the Company has also recognized another immaterial restatement item with respect to the Company's consolidated balance sheet at June 30, 2005.

The following tables show (i) selected consolidated balance sheet data as of December 31, 2004 and June 30, 2005, and selected consolidated statements of income, comprehensive income, stockholders' equity and cash flow data for the interim periods ended June 30, 2004 and 2005, in each case as previously reported, (ii) adjustments to such consolidated financial statement data to reflect the aggregate effect of this restatement and (iii) such consolidated financial statement data, as restated to reflect the aggregate effect of this restatement.

	December 31, 2004		
	Previously reported	Adjustments	As re
	-----	-----	-----
	(In thousands)		
Selected balance sheet items:			
Current receivable from affiliates	\$ 1,634 =====	\$ 47 =====	\$ =====
Total current assets	\$ 186,126 =====	\$ 47 =====	\$ 1 =====
Noncurrent deferred income taxes	\$ 45,274 =====	\$ 58,146 =====	\$ 1 =====
Total noncurrent liabilities	\$ 119,174 =====	\$ 58,146 =====	\$ 1 =====
Stockholders' equity:			
Common stock	\$ 6,054	\$ -	\$
Additional paid-in capital	417,760	(48,032)	3
Retained earnings	10,970	(10,970)	
Accumulated other comprehensive income (loss)			
Marketable securities	26,783	-	
Currency translation	(136,648)	919	(1
Pension liabilities	(33,191)	(16)	(

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

	-----	-----	-----
Total stockholders' equity	\$ 291,728	\$ (58,099)	\$ 2
	=====	=====	=====
	June 30, 2005		
	-----	-----	-----
	Previously reported	Adjustments	As re
	-----	-----	-----
		(In thousands)	
Selected balance sheet items:			
Current accrued liabilities	\$ 24,520	\$ 5,400	\$
	=====	=====	=====
Current payable to affiliates	\$ 3,413	\$ (47)	\$
	=====	=====	=====
Total current liabilities	\$ 58,012	\$ 5,353	\$
	=====	=====	=====
Noncurrent deferred income taxes	\$ 52,485	\$ 56,078	\$ 1
	=====	=====	=====
Total noncurrent liabilities	\$ 120,873	\$ 56,078	\$ 1
	=====	=====	=====
Stockholders' equity:			
Common stock	\$ 6,069	\$ -	\$
Additional paid-in capital	425,838	(53,499)	3
Retained earnings	15,402	(8,827)	
Accumulated other comprehensive income (loss)			
Marketable securities	31,012	-	
Currency translation	(135,040)	911	(1
Pension liabilities	(33,191)	(16)	(
	-----	-----	-----
Total stockholders' equity	\$ 310,090	\$ (61,431)	\$ 2
	=====	=====	=====

Three months ended
June 30, 2004

	-----	-----	-----	-----
	Previously reported	Adjustments	As restated	Previous reported
	-----	-----	-----	-----
Income from continuing operations				

(In thousands, except per share)

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

before income tax and minority interest	\$ 33,565	\$ -	\$ 33,565	\$ 47,3
Provision for income taxes (benefit)	(298,663)	43,294	(255,369)	(295,1
Minority interest in after tax earnings	142,543	-	142,543	147,8
	-----	-----	-----	-----
Income from continuing operations	189,685	(43,294)	146,391	194,7
Discontinued operations	185	-	185	1
	-----	-----	-----	-----
Net income	\$ 189,870	\$ (43,294)	\$ 146,576	\$ 194,9
	=====	=====	=====	=====
Earnings per share:				
Basic net income per share	\$ 3.93	\$ (.90)	\$ 3.03	\$ 4.
	=====	=====	=====	=====
Diluted net income per share	\$ 3.92	\$ (.89)	\$ 3.03	\$ 4.
	=====	=====	=====	=====
Weighted average shares used:				
Basic	48,361		48,361	48,2
Diluted	48,424		48,424	48,3

	Three months ended June 30, 2005			
	Previously reported	Adjustments	As restated	Previous reported
	-----	-----	-----	-----
	(In thousands, except per share)			
Income from continuing operations before income tax and minority interest	\$ 14,917	\$ -	\$ 14,917	\$ 37,2
Provision for income taxes	4,166	81	4,247	12,2
Minority interest in after tax earnings	785	-	785	1,5
	-----	-----	-----	-----
Income (loss) from continuing operations	9,966	(81)	9,885	23,4
Discontinued operations	-	-	-	(3
	-----	-----	-----	-----
Net income	\$ 9,966	\$ (81)	\$ 9,885	\$ 23,1
	=====	=====	=====	=====
Earnings per share:				
Basic net income per share	\$.20	\$ -	\$.20	\$.

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

	=====	=====	=====	=====
Diluted net income per share	\$.20	\$ -	\$.20	\$.
	=====	=====	=====	=====
Weighted average shares used:				
Basic	48,553		48,553	48,5
Diluted	48,593		48,593	48,5

	Six months ended June 30, 2004		
	-----		-----
	Previously reported	Adjustments ----- (In thousands)	As re -----
Consolidated other comprehensive income:			
Net income	\$ 194,954	\$ (42,881)	\$ 1
	=====	=====	=====
Other comprehensive income, net of tax:			
Marketable securities adjustment	(11,082)	-	(
Currency translation adjustment	(4,014)	1,036	-----
	-----	-----	-----
Total other comprehensive income	(15,096)	1,036	(
	-----	-----	-----
Comprehensive income	\$ 179,858	\$ (41,845)	\$ 1
	=====	=====	=====

	Six months June 30, 2005		
	-----		-----
	Previously reported	Adjustments ----- (In thousands)	As re -----
Consolidated other comprehensive income:			
Net income	\$ 23,145	\$ 1,230	\$
	=====	=====	=====
Other comprehensive income, net of tax:			
Marketable securities adjustment	4,229	-	-----
Currency translation adjustment	1,608	(8)	-----
	-----	-----	-----
Total other comprehensive income	5,837	(8)	-----

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

	-----	-----	---
Comprehensive income	\$ 28,982	\$ 1,222	\$
	=====	=====	===

Total stockholders equity -
Six months ended June 30, 2005

	Previously reported	Adjustments	As re
	-----	-----	-----
Balance at December 31, 2004	\$ 291,728	\$ (58,099)	\$ 2
Net income	23,145	1,230	
Other comprehensive income, net	5,837	(8)	
Income tax on distribution	(3,937)	913	
Other, net	(6,683)	(5,467)	(
	-----	-----	---
Balance at June 30, 2005	\$ 310,090	\$ (61,431)	\$ 2
	=====	=====	===

Six months ended June 30, 2004

	Previously reported	Adjustments	As re
	-----	-----	-----
Items comprising cash flow from operating activities:			
Net income	\$ 194,954	\$ (42,881)	\$ 1
	=====	=====	===
Deferred income taxes from continuing operations	\$ (306,260)	\$ 42,494	\$ (2
	=====	=====	===
Accounts with affiliates	\$ 306	\$ 387	\$
	=====	=====	===
Net cash provided by operating activities	\$ 71,617	\$ -	\$
	=====	=====	===

Six months ended June 30, 2005

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

	----- Previously reported -----	Adjustments -----	As re -----
Items comprising cash flow from operating activities:			
Net income	\$ 23,145 =====	\$ 1,230 =====	\$ =====
Deferred income taxes from continuing operations	\$ (12,540) =====	\$ (2,143) =====	\$ (=====
Accounts with affiliates	\$ 2,864 =====	\$ 913 =====	\$ =====
Net cash used by operating activities	\$ (18,113) =====	\$ - =====	\$ (=====

In addition, during the fourth quarter of 2004, Kronos determined that it should have recognized an additional \$17.3 million net deferred income tax benefit during the second quarter of 2004, primarily related to the amount of the valuation allowance related to Kronos' German operations which should have been reversed. The Company's results of operations for the six months ended June 30, 2004, as presented herein, reflects this additional income tax benefit, which aggregated \$8.7 million, or \$.18 per diluted share, net of minority interest.

As previously disclosed, on May 9, 2005 the Company and its audit committee also concluded to restate the Company's consolidated financial statements as of December 31, 2004 and for the year then ended, to reflect an additional \$4.2 million, or \$.08 per diluted share, noncash deferred income tax benefit in its results of operations for the year ended December 31, 2004. Such \$4.2 million relates to recognition of an additional noncash deferred income tax benefit related to discontinued operations in the fourth quarter of 2004. This restatement was included in the Company's Amendment No. 1 on Form 10-K/A of the Company's Annual Report on Form 10-K for the year ended December 31, 2004, filed with the SEC on May 31, 2005. The previously-reported amounts shown in the tables above reflect, as applicable, the effect of this \$4.2 million restatement.

Organization and basis of presentation

NL Industries, Inc. (NYSE: NL) is a subsidiary of Valhi, Inc. (NYSE: VHI). At June 30, 2005, Valhi held approximately 83% of NL's outstanding common stock and Contran Corporation and its subsidiaries held approximately 91% of Valhi's outstanding common stock. Substantially all of Contran's outstanding voting stock is held by trusts established for the benefit of certain children and grandchildren of Harold C. Simmons, of which Mr. Simmons is sole trustee, or is held by Mr. Simmons or persons or other entities related to Mr. Simmons. Consequently, Mr. Simmons may be deemed to control each of such companies.

The consolidated balance sheet of NL Industries, Inc. and Subsidiaries (collectively, the "Company") as of December 31, 2004 has been derived from the Company's audited consolidated financial statements at that date included in its

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Annual Report on Form 10-K for the year ended December 31, 2004 filed on March 30, 2005, as amended by Amendment No. 1 on Form 10-K/A filed on May 31, 2005 and as further amended by Amendment No. 2 on Form 10-K/A filed with the SEC on December 22, 2005 (the "2004 Annual Report").

On September 24, 2004, the Company completed the acquisition of 10,374,000 shares of CompX International Inc. (NYSE: CIX) common stock, representing approximately 68% of the outstanding shares of CompX common stock. NL's acquisition was accounted for under GAAP as a transfer of net assets among entities under common control, and accordingly resulted in a change in reporting entity. The Company has retroactively restated its consolidated financial statements to reflect the consolidation of CompX for all periods presented.

The consolidated balance sheet at June 30, 2005, and the consolidated statements of income, comprehensive income (loss), stockholders' equity and cash flows for the interim periods ended June 30, 2004 and 2005, have been prepared by the Company, without audit, in accordance with GAAP. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary to state fairly the consolidated financial position, results of operations and cash flows have been made. The results of operations for the interim periods are not necessarily indicative of the operating results for a full year or of future operations. Certain information normally included in financial statements prepared in accordance with GAAP has been condensed or omitted. The accompanying consolidated financial statements should be read in conjunction with the 2004 Annual Report.

Other

Prior to July 2004, Kronos Worldwide, Inc. (NYSE: KRO) was a majority-owned subsidiary of the Company. Following the Company's July 2004 dividend in the form of shares of Kronos common stock distributed to NL shareholders, the Company's ownership of Kronos was reduced to less than 50%. Consequently, effective July 1, 2004 the Company ceased to consolidate Kronos' financial position, results of operations and cash flows and the Company commenced accounting for its interest in Kronos by the equity method. The Company continues to report Kronos as a consolidated subsidiary through June 30, 2004, including the consolidation of Kronos' results of operations and cash flows for the second quarter and first six months of 2004.

As disclosed in the 2004 Annual Report, the Company accounts for stock-based employee compensation in accordance with Accounting Principles Board Opinion ("APBO") No. 25, "Accounting for Stock Issued to Employees," and its various interpretations. See Note 16. Under APBO No. 25, no compensation cost is generally recognized for fixed stock options in which the exercise price is greater than or equal to the market price on the grant date. Prior to 2004, and following the cash settlement of certain stock options held by employees of NL, the Company commenced accounting for its stock options using the variable accounting method of APBO No. 25 because NL could not overcome the presumption that it would not similarly cash settle its remaining stock options. Under the variable accounting method, the intrinsic value of all unexercised stock options (including stock options with an exercise price at least equal to the market price on the date of grant) is accrued as an expense, with subsequent increases (decreases) in the Company's market price resulting in the recognition of additional compensation expense (income). Net compensation cost recognized by the Company in accordance with APBO No. 25 was nil in the second quarter of 2004, and approximately \$1.1 million in the first six months of 2004. Net compensation income recognized by the Company was approximately \$400,000 in both the second quarter and first six months of 2005.

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

The following table presents what the Company's consolidated net income, and related per share amounts, would have been in the second quarter and first six months of 2004 and 2005 if the Company and its subsidiaries and affiliates had each elected to account for their respective stock-based employee compensation related to stock options in accordance with the fair value-based recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, "Accounting for Stock-Based Compensation," for all awards granted subsequent to January 1, 1995.

	Three months ended		Six months e
	June 30,		June 30,
	2004	2005	2004
	-----	-----	-----
	(Restated)	(Restated)	(Restated)
	(In millions, except per share amount)		
Net income as reported	\$146.6	\$ 9.9	\$152.1
Adjustments, net of applicable income tax effects and minority interest:			
Stock-based employee compensation expense determined under APBO No. 25	-	(.3)	.6
Stock-based employee compensation expense determined under SFAS No. 123	(.2)	-	(.3)
	-----	-----	-----
Pro forma net income	\$146.4	\$ 9.6	\$152.4
	=====	=====	=====
Diluted net income per share:			
As reported	\$ 3.03	\$.20	\$ 3.15
Pro forma	\$ 3.02	\$.20	\$ 3.15

Note 2 - Business segment information:

Business segment	Entity	% owned at June 30, 2005
-----	-----	-----
Component products	CompX International Inc.	68%
Chemicals	Kronos Worldwide, Inc.	36%

The Company's ownership of CompX is directly held principally by CompX Group, Inc., an 82.4%-owned subsidiary of the Company. An affiliate of Valhi owns the remaining 17.6% of CompX Group. CompX Group's sole asset consists of shares of CompX common stock representing approximately 83% of the total number of CompX shares outstanding, and the percentage ownership of CompX shown above includes NL's ownership interest in CompX Group multiplied by CompX Group's ownership interest in CompX. During the second quarter of 2005, NL purchased approximately 39,000 shares of CompX common stock in open market transactions, representing approximately .3% of CompX's outstanding common stock for an aggregate amount of approximately \$572,000.

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

In March 2005, NL paid its \$.25 per share regular quarterly dividend in the form of shares of Kronos common stock in which approximately 266,000 shares, or approximately .5% of Kronos' outstanding common stock, were distributed to NL shareholders in the form of a pro-rata dividend. NL's distribution of such shares of Kronos common stock is taxable to NL, and NL is required to recognize a taxable gain equal to the difference between the fair market value of the shares of Kronos common stock distributed and NL's adjusted tax basis in such stock at the date of distribution. The Company recognized an aggregate \$3.9 million tax liability in the first quarter of 2005 related to the Kronos shares distributed. In accordance with GAAP, the amount of such income tax represented by the excess of the carrying value of such stock for financial reporting purposes and the adjusted tax basis of such stock is included in the determination of net income in the period the shares were distributed, and the amount of such income tax represented by the excess of the fair market value of such stock and the carrying value of such stock for financial reporting purposes is accounted for as a direct reduction to the Company's stockholders' equity (retained earnings). The amount of such income tax included in the determination of net income aggregated \$913,000, while the amount of such income tax accounted for as a direct reduction to equity aggregated \$3.0 million.

During the first six months of 2005, NL sold approximately 470,000 shares of Kronos common stock in market transactions for an aggregate of \$19.2 million. The Company recognized a \$14.7 million pre-tax securities transaction gain related to such sales.

CompX (NYSE: CIX) and Kronos (NYSE: KRO) each file periodic reports with the SEC pursuant to the Securities Exchange Act of 1934, as amended.

A summary of sales and segment profit for the Company's business segments during the 2004 and 2005 interim periods, and other items included in the determination of income from continuing operations before income taxes and minority interest, are presented in the following table.

	Three months ended June 30,		Six months e June 30,
	2004	2005	2004
	-----	-----	-----
	(In millions)		
Net sales:			
Chemicals	\$295.8	\$ -	\$559.1
Component products	46.2	45.8	89.8
	-----	-----	-----
Total net sales	\$342.0	\$45.8	\$648.9
	=====	=====	=====
Segment profit:			
Chemicals	\$ 40.1	\$ -	\$ 66.3
Component products	5.1	4.7	7.6
	-----	-----	-----
Total segment profit	45.2	4.7	73.9
General corporate items:			

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Interest and dividend income from affiliates	.8	.6	1.7
Other interest income	.4	.8	.7
Securities transactions, net	-	.1	-
Insurance recoveries	.5	1.2	.5
Other income	.1	.1	.1
General corporate expenses, net	(4.6)	(4.3)	(11.3)
Interest expense	(8.8)	(.1)	(18.2)
	-----	-----	-----
	33.6	3.1	47.4
Equity in earnings of Kronos	-	11.8	-
	-----	-----	-----
Income from continuing operations before income taxes and minority interest	\$ 33.6	\$14.9	\$ 47.4
	=====	=====	=====

Component products segment profit, as presented above, may differ from amounts separately reported by CompX because the Company defines segment profit differently than CompX.

Note 3 - Accounts and other receivables:

	December 31, 2004	June 30, 2005
	-----	-----
	(In thousands)	
Trade receivables	\$ 24,759	\$ 21,577
Recoverable VAT and other receivables	551	2,001
Allowance for doubtful accounts	(1,008)	(255)
	-----	-----
	\$ 24,302	\$ 23,323
	=====	=====

Note 4 - Inventories:

	December 31, 2004	June 30, 2005
	-----	-----
	(In thousands)	
Raw materials	\$ 8,193	\$ 4,286
Work in process	10,827	9,560
Finished products	9,696	6,029
Supplies	65	70
	-----	-----
	\$ 28,781	\$ 19,945
	=====	=====

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Note 5 - Marketable equity securities:

	December 31, 2004	June 30, 2005
	-----	-----
	(In thousands)	
Valhi common stock	\$ 75,770	\$ 82,410
Other	23	27
	-----	-----
	\$ 75,793	\$ 82,437
	=====	=====

At June 30, 2005, the Company owned approximately 4.7 million shares of Valhi common stock with a quoted market price of \$17.50 per share (December 31, 2004 quoted market price - \$16.09 per share).

Note 6 - Investment in Kronos:

At June 30, 2005, the Company held 17.5 million shares of Kronos with a quoted market price of \$30.19 per share, or an aggregate market value of \$529 million.

Securities transaction gains in the first six months of 2005 relate primarily to NL's \$14.7 million pre-tax gain from the sale of approximately 470,000 shares of Kronos common stock in market transactions for aggregate proceeds of \$19.2 million.

At June 30, 2005, Kronos reported total assets of \$1.3 billion and stockholders' equity of \$505.4 million. Kronos' total assets at June 30, 2005 include current assets of \$484.0 million, net property and equipment of \$414.3 million and an investment in a TiO2 manufacturing joint venture of \$119.6 million. Kronos' total liabilities at June 30, 2005 include current liabilities of \$173.3 million, long-term debt of \$461.2 million, accrued postretirement benefits and pension costs aggregating \$67.1 million and deferred income taxes of \$58.2 million.

During the three months ended June 30, 2005, Kronos reported net sales of \$311.7 million, income from operations of \$57.7 million and net income of \$32.9 million. During the six months ended June 30, 2005, Kronos reported net sales of \$603.6 million, income from operations of \$104.1 million and net income of \$54.3 million.

Note 7 - Other noncurrent assets:

	December 31, 2004	June 30, 2005
	-----	-----
	(In thousands)	
Intangible assets	\$ 3,190	\$ 2,892
Note receivable	-	4,179

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Other	525	434
	-----	-----
	\$ 3,715	\$ 7,505
	=====	=====

The note receivable relates to part of the consideration received by CompX from the January 2005 sale of its Thomas Regout operations in Europe. See Note 15.

Note 8 - Accrued liabilities:

	December 31, 2004	June 30, 2005
	-----	-----
(In thousands)		
Employee benefits	\$ 14,775	\$ 11,899
Other	8,359	18,021
	-----	-----
	\$ 23,134	\$ 29,920
	=====	=====

Note 9 - Other noncurrent liabilities:

	December 31, 2004	June 30, 2005
	-----	-----
(In thousands)		
Insurance	\$ 2,507	\$ 2,587
Other	1,521	515
	-----	-----
	\$ 4,028	\$ 3,102
	=====	=====

Note 10 - Minority interest:

	December 31, 2004	June 30, 2005
	-----	-----
(In thousands)		
Minority interest in net assets:		
CompX International Inc.	\$ 49,154	\$ 49,274
NL Environmental Management Services, Inc.	9,250	-

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

-----	-----
\$ 58,404	\$ 49,274
=====	=====

Three months ended June 30,		Six months ended June 30,
-----	-----	-----
2004	2005	2004
----	----	----
(In thousands)		

Minority interest in net earnings:

Kronos Worldwide, Inc.	\$141,051	\$ -	\$145,837
CompX International Inc.	943	753	1,431
NL Environmental Management Services, Inc.	537	32	537
Subsidiary of Kronos Worldwide, Inc.	12	-	20
	-----	-----	-----
	\$142,543	\$ 785	\$147,825
	=====	=====	=====

In June 2005, NL's majority-owned subsidiary, NL Environmental Management Services, Inc. ("EMS"), received notices from the three minority shareholders of EMS indicating they were each exercising their right, which became exercisable on June 1, 2005, to require EMS to purchase their shares in EMS as of June 30, 2005 for a formula-determined amount as provided in EMS' certificate of incorporation. In accordance with the certificate of incorporation, EMS made a determination in good faith of the amount payable to the three former minority shareholders to purchase their shares of EMS stock, which amount may be subject to review by a third party. In June 2005, EMS set aside funds as payment for the shares of EMS, but as of June 30, 2005 the former minority shareholders have not tendered their shares, and accordingly the liability owed to these former minority shareholders, which has not been extinguished for financial reporting purposes as of June 30, 2005, is classified as a current liability at such date. Similarly, the funds which have been set aside are classified as a current asset at such date.

Note 11 - Other income:

Six months ended June 30,	
-----	-----
2004	2005
----	----
(In thousands)	

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Insurance recoveries	\$ 495	\$ 1,200
Contract dispute settlement	6,289	-
Other	160	243
	-----	-----
	\$ 6,944	\$ 1,443
	=====	=====

Insurance recoveries in the first six months of 2005 relate to NL's expected recovery from certain insolvent former insurance carriers relating to settlement of excess insurance coverage claims. Such amount was received by NL in August 2005.

Note 12 - Provision for income taxes:

	Six months ended	
	2004	2005
	-----	-----
	(Restated)	(Restated)
	(In millions)	
Expected tax expense	\$ 16.6	\$ 13.0
Non-U.S. tax rates	(.2)	(.1)
Incremental U.S. tax and rate differences on equity in earnings	48.5	(4.6)
Change in deferred income tax valuation allowance, net	(308.4)	-
Nondeductible expenses	1.9	.2
U.S. state income taxes, net	.3	.1
Refund of prior year German income taxes	(3.1)	-
Excess of book basis over tax basis of Kronos common stock sold or distributed	.4	2.4
Tax contingency reserve adjustment, net	(18.1)	.2
Other, net	9.8	(.2)
	-----	-----
	\$ (252.3)	\$ 11.0
	=====	=====

Certain U.S. and non-U.S. tax returns of the Company and Kronos are being examined and tax authorities have or may propose tax deficiencies, including penalties and interest. For example:

- o Kronos has received a preliminary tax assessment related to 1993 from the Belgian tax authorities proposing tax deficiencies, including related interest, of approximately euro 6 million (\$7 million at June 30, 2005). Kronos has filed a protest to this assessment, and believes that a significant portion of the assessment is without merit. The Belgian tax authorities have filed a lien on the fixed assets of Kronos' Belgian TiO2 operations in connection with this assessment. In April 2003, Kronos received a notification from the Belgian tax authorities of their intent to assess a tax deficiency related to 1999 that, including interest, is

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

expected to be approximately euro 9 million (\$11 million). Kronos believes the proposed assessment is substantially without merit, and Kronos has filed a written response.

- o The Norwegian tax authorities have notified Kronos of their intent to assess tax deficiencies of approximately kroner 12 million (\$2 million) relating to the years 1998 through 2000. Kronos has objected to this proposed assessment.
- o Kronos has received a preliminary tax assessment from the Canadian tax authorities related to the years 1998 and 1999 proposing tax deficiencies, including interest, of Cdn. \$5 million (\$4 million). Kronos has filed a protest and believes a significant portion of the assessment is without merit.

No assurance can be given that these unresolved tax matters will be resolved in the Company's or Kronos' favor in view of the inherent uncertainties involved in settlement initiatives, and court and tax proceedings. The Company believes that it has provided adequate accruals for additional taxes and related interest expense which may ultimately result from all such examinations and believes that the ultimate disposition of such examinations should not have a material adverse effect on its consolidated financial position, results of operations or liquidity.

Note 13 - Employee benefit plans:

The components of net periodic defined benefit pension cost (income) are presented in the table below.

	Three months ended June 30,		Six months ended June 30,
	2004	2005	2004

	(In thousands)		
Service cost	\$ 1,459	\$ -	\$ 3,128
Interest cost	4,989	758	10,020
Expected return on plan assets	(4,678)	(1,014)	(9,400)
Amortization of prior service cost	140	-	281
Amortization of net transition obligations and assets	147	(18)	290
Recognized actuarial losses	966	98	1,928
	-----	-----	-----
	\$ 3,023	\$ (176)	\$ 6,247
	=====	=====	=====

The components of net periodic postretirement benefits other than pensions ("OPEB") cost are presented in the table below.

	Three months ended June 30,		Six months ended June 30,
	2004	2005	2004

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

(In thousands)

Service cost	\$ 56	\$ -	\$ 113
Interest cost	469	211	940
Amortization of prior service credit	(256)	(71)	(511)
Recognized actuarial losses	70	-	141
	-----	-----	-----
	\$ 339	\$ 140	\$ 683
	=====	=====	=====

Note 14 - Commitments and contingencies:

Lead pigment litigation. NL's former operations included the manufacture of lead pigments for use in paint and lead-based paint. NL, other former manufacturers of lead pigments for use in paint and lead-based paint (together, the "former pigment manufacturers"), and the Lead Industries Association ("LIA"), which discontinued business operations in 2002, have been named as defendants in various legal proceedings seeking damages for personal injury, property damage and governmental expenditures allegedly caused by the use of lead-based paints. Certain of these actions have been filed by or on behalf of states, large U.S. cities or their public housing authorities and school districts, and certain others have been asserted as class actions. These lawsuits seek recovery under a variety of theories, including public and private nuisance, negligent product design, negligent failure to warn, strict liability, breach of warranty, conspiracy/concert of action, aiding and abetting, enterprise liability, market share or risk contribution liability, intentional tort, fraud and misrepresentation, violations of state consumer protection statutes, supplier negligence and similar claims.

The plaintiffs in these actions generally seek to impose on the defendants responsibility for lead paint abatement and health concerns associated with the use of lead-based paints, including damages for personal injury, contribution and/or indemnification for medical expenses, medical monitoring expenses and costs for educational programs. A number of cases are inactive or have been dismissed or withdrawn. Most of the remaining cases are in various pre-trial stages. Some are on appeal following dismissal or summary judgment rulings in favor of the defendants. In addition, various other cases are pending (in which NL is not a defendant) seeking recovery for injury allegedly caused by lead pigment and lead-based paint. Although NL is not a defendant in these cases, the outcome of these cases may have an impact on cases that might be filed against NL in the future.

NL believes these actions are without merit, intends to continue to deny all allegations of wrongdoing and liability and to defend against all actions vigorously. NL has neither lost nor settled any of these cases. NL has not accrued any amounts for pending lead pigment and lead-based paint litigation. Liability that may result, if any, cannot reasonably be estimated. There can be no assurance that NL will not incur liability in the future in respect of this pending litigation in view of the inherent uncertainties involved in court and jury rulings in pending and possible future cases. If any such future liability were to be incurred, it could have a material adverse effect on the Company's consolidated financial position, results of operations and liquidity.

NL has reached an agreement with one of its former insurance carriers in which such carrier would reimburse NL for a portion of its past and future lead pigment litigation defense costs, although the amount which NL will ultimately recover from such carrier with respect to such defense costs incurred by NL is not yet determinable. NL is also continuing discussions with another former insurance carrier with respect to recovery of past and future defense costs. In

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

addition, during the second quarter of 2005, NL recognized \$1.2 million of expected recoveries from certain insolvent former insurance carriers relating to settlement of excess insurance claims. While NL continues to seek additional recoveries of past defense costs as well as an agreement related to future defense costs, there can be no assurance that NL will be successful in obtaining reimbursement for either defense costs or indemnity. NL has not considered any potential insurance recoveries in determining related accruals for lead pigment litigation matters. Any such additional insurance recoveries would be recognized when their receipt is deemed probable and the amount is determinable.

Environmental matters and litigation. The Company's operations are governed by various environmental laws and regulations. Certain of the Company's businesses are and have been engaged in the handling, manufacture or use of substances or compounds that may be considered toxic or hazardous within the meaning of applicable environmental laws. As with other companies engaged in similar businesses, certain past and current operations and products of the Company have the potential to cause environmental or other damage. The Company has implemented and continues to implement various policies and programs in an effort to minimize these risks. The Company's policy is to maintain compliance with applicable environmental laws and regulations at all of its plants and to strive to improve environmental performance. From time to time, the Company may be subject to environmental regulatory enforcement under U.S. and foreign statutes, resolution of which typically involves the establishment of compliance programs. It is possible that future developments, such as stricter requirements of environmental laws and enforcement policies thereunder, could adversely affect the Company's production, handling, use, storage, transportation, sale or disposal of such substances. The Company believes all of its plants are in substantial compliance with applicable environmental laws.

Certain properties and facilities used in the Company's former businesses, including divested primary and secondary lead smelters and former mining locations of NL, are the subject of civil litigation, administrative proceedings or investigations arising under federal and state environmental laws. Additionally, in connection with past disposal practices, the Company has been named as a defendant, potential responsible party ("PRP") or both, pursuant to the Comprehensive Environmental Response, Compensation and Liability Act, as amended by the Superfund Amendments and Reauthorization Act ("CERCLA"), and similar state laws in various governmental and private actions associated with waste disposal sites, mining locations, and facilities currently or previously owned, operated or used by the Company or its subsidiaries, or their predecessors, certain of which are on the U.S. EPA's Superfund National Priorities List or similar state lists. These proceedings seek cleanup costs, damages for personal injury or property damage and/or damages for injury to natural resources. Certain of these proceedings involve claims for substantial amounts. Although the Company may be jointly and severally liable for such costs, in most cases it is only one of a number of PRPs who may also be jointly and severally liable.

Environmental obligations are difficult to assess and estimate for numerous reasons including the complexity and differing interpretations of governmental regulations, the number of PRPs and the PRPs' ability or willingness to fund such allocation of costs, their financial capabilities and the allocation of costs among PRPs, the solvency of other PRPs, the multiplicity of possible solutions, and the years of investigatory, remedial and monitoring activity required. In addition, the imposition of more stringent standards or requirements under environmental laws or regulations, new developments or changes respecting site cleanup costs or allocation of such costs among PRPs, solvency of other PRPs, the results of future testing and analysis undertaken with respect to certain sites or a determination that the Company is potentially responsible for the release of hazardous substances at other sites, could result in expenditures in excess of amounts currently estimated by the Company to be required for such matters. In addition, with respect to other PRPs and the fact

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

that the Company may be jointly and severally liable for the total remediation cost at certain sites, the Company could ultimately be liable for amounts in excess of its accruals due to, among other things, reallocation of costs among PRPs or the insolvency of one or more PRPs. No assurance can be given that actual costs will not exceed accrued amounts or the upper end of the range for sites for which estimates have been made and no assurance can be given that costs will not be incurred with respect to sites as to which no estimate presently can be made. Further, there can be no assurance that additional environmental matters will not arise in the future. If any such future liability were to be incurred, it could have a material adverse effect on the Company's consolidated financial statements, results of operations and liquidity.

The Company records liabilities related to environmental remediation obligations when estimated future expenditures are probable and reasonably estimable. Such accruals are adjusted as further information becomes available or circumstances change. Estimated future expenditures are generally not discounted to their present value. Recoveries of remediation costs from other parties, if any, are recognized as assets when their receipt is deemed probable. At June 30, 2005, no receivables for recoveries had been recognized.

The exact time frame over which the Company makes payments with respect to its accrued environmental costs is unknown and is dependent upon, among other things, the timing of the actual remediation process which in part depends on factors outside the control of the Company. At each balance sheet date, the Company makes an estimate of the amount of its accrued environmental costs which will be paid out over the subsequent 12 months, and the Company classifies such amount as a current liability. The remainder of the accrued environmental costs is classified as a noncurrent liability.

A summary of the activity in the Company's accrued environmental costs during the first six months of 2005 is presented in the table below.

	Amount

	(In thousands)
Balance at the beginning of the period	\$ 67,817
Additions charged to expense	2,976
Payments	(5,977)

Balance at the end of the period	\$ 64,816
	=====
Amounts recognized in the balance sheet	
at the end of the period:	
Current liability	\$ 16,688
Noncurrent liability	48,128

	\$ 64,816
	=====

On a quarterly basis, the Company evaluates the potential range of its liability at sites where it has been named as a PRP or defendant, including sites for which EMS has contractually assumed the Company's obligation. At June

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

30, 2005, the Company had accrued \$64.8 million for those environmental matters which the Company believes are reasonably estimable. The Company believes it is not possible to estimate the range of costs for certain sites. The upper end of the range of reasonably possible costs to the Company for sites for which the Company believes it is possible to estimate costs is approximately \$99 million. The Company's estimates of such liabilities have not been discounted to present value.

At June 30, 2005, there are approximately 20 sites for which the Company is unable to estimate a range of costs. For these sites, generally the investigation is in the early stages, and it is either unknown as to whether or not the Company actually had any association with the site, or if the Company had association with the site, the nature of its responsibility, if any, for the contamination at the site and the extent of contamination. The timing on when information would become available to the Company to allow the Company to estimate a range of loss is unknown and dependent on events outside the control of the Company, such as when the party alleging liability provides information to the Company.

At June 30, 2005, the Company had \$3 million in restricted cash, restricted cash equivalents and restricted marketable debt securities held by special purpose trusts, the assets of which can only be used to pay for certain of the Company's future environmental remediation and other environmental expenditures (December 31, 2004 - \$8 million). Use of such restricted balances does not affect the Company's consolidated net cash flows.

Other litigation. Reference is made to the 2004 Annual Report for a discussion of certain other legal proceedings to which the Company is a party.

NL has been named as a defendant in various lawsuits in a variety of jurisdictions, alleging personal injuries as a result of occupational exposure primarily to products manufactured by formerly-owned operations of NL containing asbestos, silica and/or mixed dust. Approximately 490 of these types of cases involving a total of approximately 14,500 plaintiffs and their spouses remain pending. NL has not accrued any amounts for this litigation because liability that might result to NL, if any, cannot be reasonably estimated. To date, NL has not been adjudicated liable in any of these matters. Based on information available to NL, including facts concerning its historical operations, the rate of new claims, the number of claims from which NL has been dismissed and NL's prior experience in the defense of these matters, NL believes that the range of reasonably possible outcomes of these matters will be consistent with NL's historical costs with respect to these matters (which are not material), and no reasonably possible outcome is expected to involve amounts that are material to NL. NL has and will continue to vigorously seek dismissal from each claim and/or a finding of no liability by NL in each case. In addition, from time to time, NL has received notices regarding asbestos or silica claims purporting to be brought against former subsidiaries of NL, including notices provided to insurers with which NL has entered into settlements extinguishing certain insurance policies. These insurers may seek indemnification from NL.

In addition to the litigation described above, the Company and its affiliates are also involved in various other environmental, contractual, product liability, patent (or intellectual property), employment and other claims and disputes incidental to its present and former businesses. In certain cases, the Company has insurance coverage for such items; however the Company does not currently expect additional material insurance coverage for environmental claims.

The Company currently believes that the disposition of all claims and disputes, individually or in the aggregate, should not have a material adverse

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

effect on its consolidated financial position, results of operations or liquidity.

Note 15 - Discontinued operations:

As discussed in the 2004 Annual Report, in December 2004 CompX's board of directors committed to a formal plan to dispose of its Thomas Regout operations in the Netherlands. Such operations, which previously were included in the Company's component products operating segment (see Note 2), met all of the criteria under GAAP to be classified as an asset held for sale at December 31, 2004, and accordingly the results of operations of Thomas Regout have been classified as discontinued operations for all periods presented. The Company has not reclassified its consolidated balance sheet as of December 31, 2004 or its 2004 statement of cash flows. In classifying the net assets of the Thomas Regout operations as an asset held for sale, the Company concluded that the carrying amount of the net assets of such operations exceeded the estimated fair value less costs to sell of such operations, and accordingly in the fourth quarter of 2004 the Company recognized a \$6.5 million impairment charge to write-down its investment in the Thomas Regout operations to its estimated net realizable value. Such charge represented an impairment of goodwill.

In January 2005, CompX completed the sale of such operations for proceeds (net of expenses) of approximately \$22.3 million. The net proceeds consisted of approximately \$18.1 million in cash at the date of sale and a \$4.2 million principal amount note receivable from the purchaser bearing interest at a fixed rate of 7% and payable over four years. The note receivable is collateralized by a secondary lien on the assets sold and is subordinated to certain third-party indebtedness of the purchaser. Accordingly, the Company no longer includes the results of operations or cash flows of Thomas Regout subsequent to December 31, 2004 in its consolidated financial statements. The net proceeds from the January 2005 sale of Thomas Regout were approximately \$860,000 less than the net realizable value estimated at the time of the goodwill impairment charge (primarily due to higher expenses associated with the disposal of the Thomas Regout operations), and discontinued operations in the first quarter of 2005 includes a charge related to such differential (\$326,000 loss, net of income tax benefit and minority interest). During the first six months of 2004, the Thomas Regout operations reported net sales of \$20.6 million, income from operations of \$1.2 million, interest expense of \$800,000 and net income of \$300,000 (approximately \$200,000 to NL, net of minority interest).

Note 16 - Accounting principles not yet implemented:

Inventory costs. The Company will adopt SFAS No. 151, "Inventory Costs, an amendment of ARB No. 43, Chapter 4," for inventory costs incurred on or after January 1, 2006. SFAS No. 151 requires that the allocation of fixed production overhead costs to inventory shall be based on normal capacity. Normal capacity is not defined as a fixed amount; rather, normal capacity refers to a range of production levels expected to be achieved over a number of periods under normal circumstances, taking into account the loss of capacity resulting from planned maintenance shutdowns. The amount of fixed overhead allocated to each unit of production is not increased as a consequence of idle plant or production levels below the low end of normal capacity, but instead a portion of fixed overhead costs is charged to expense as incurred. Alternatively, in periods of production above the high end of normal capacity, the amount of fixed overhead costs allocated to each unit of production is decreased so that inventories are not measured above cost. SFAS No. 151 also clarifies existing GAAP to require that abnormal freight and wasted materials (spoilage) are to be expensed as incurred. The Company believes its production cost accounting already complies with the requirements of SFAS No. 151, and the Company does not expect adoption of SFAS No. 151 will have a material effect on its consolidated financial statements.

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Stock options. As permitted by regulations of the SEC the Company will adopt SFAS No. 123R, "Share-Based Payment," as of January 1, 2006. SFAS No. 123R, among other things, eliminates the alternative in existing GAAP to use the intrinsic value method of accounting for stock-based employee compensation under APBO No. 25. Upon adoption of SFAS No. 123R, the Company will generally be required to recognize the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award, with the cost recognized over the period during which an employee is required to provide services in exchange for the award (generally, the vesting period of the award). No compensation cost will be recognized in the aggregate for equity instruments for which the employee does not render the requisite service (generally, the instrument is forfeited before it has vested). The grant-date fair value will be estimated using option-pricing models (e.g. Black-Scholes or a lattice model). Under the transition alternatives permitted under SFAS No. 123R, the Company will apply the new standard to all new awards granted on or after January 1, 2006, and to all awards existing as of December 31, 2005 which are subsequently modified, repurchased or cancelled. Additionally, as of January 1, 2006, the Company will be required to recognize compensation cost previously measured under SFAS No. 123 for the portion of any non-vested award existing as of December 31, 2005 over the remaining vesting period. Because the number of non-vested awards as of December 31, 2005 with respect to options granted by NL is not expected to be material, and because the Company has not granted any options and does not expect to grant any options prior to January 1, 2006, the effect of adopting SFAS No. 123R is not expected to be significant in so far as it relates to existing stock options. Should NL or its subsidiaries and affiliates, however, either grant a significant number of options or modify, repurchase or cancel existing options in the future, the effect on the Company's consolidated financial statements could be material.

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

RESULTS OF OPERATIONS:

General

The Company reported net income of \$9.9 million, or \$.20 per diluted share, in the second quarter of 2005 compared to net income of \$146.6 million, or \$3.03 per diluted share, in the second quarter of 2004. For the first six months of 2005, the Company reported net income of \$24.4 million, or \$.50 per diluted share, compared to net income of \$152.1 million, or \$3.15 per diluted share, in the first six months of 2004. (See Note 1 to the Consolidated Financial Statements.) As discussed in Note 1 to the Consolidated Financial Statements, the Company's consolidated financial statements have been restated.

The decrease in the Company's diluted earnings per share from the second quarter and first six months of 2004 to the second quarter and first six months of 2005 is due primarily to the net effects of (i) higher component products segment profit, (ii) higher earnings attributable to Kronos' income from operations, (iii) security transactions gains from the sale of shares of Kronos common stock in 2005 and (iv) a significant second quarter 2004 income tax benefit related to Kronos. The Company currently believes its net income in 2005 will be lower than 2004 due primarily to the effect of such second quarter 2004 income tax benefits related to Kronos.

As discussed in Note 1 to the Consolidated Financial Statements, on

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

September 24, 2004, the Company purchased 10,374,000 shares of CompX common stock, representing approximately 68% of the outstanding shares of CompX common stock, from Valhi and a wholly-owned subsidiary of Valhi. Because Valhi, NL and CompX are all entities under the common control of Contran, the Company's acquisition of the shares of CompX common stock results in a change in reporting entity and the Company has retroactively restated its consolidated financial statements to reflect the consolidation of CompX for all periods presented.

Also discussed in Note 1, prior to July 2004, Kronos was a majority-owned subsidiary of the Company. Following the Company's July 2004 dividend in the form of shares of Kronos common stock distributed to NL shareholders, the Company's ownership of Kronos was reduced to less than 50%. Consequently, effective July 1, 2004 the Company ceased to consolidate Kronos' financial position, results of operations and cash flows and the Company commenced accounting for its interest in Kronos by the equity method. The Company continues to report Kronos as a consolidated subsidiary through June 30, 2004, including the consolidation of Kronos' results of operations and cash flows for the second quarter and first six months of 2004.

As provided by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, the Company cautions that the statements in this Quarterly Report on Form 10-Q relating to matters that are not historical facts, are forward-looking statements that represent management's beliefs and assumptions based on currently available information. Forward-looking statements can be identified by the use of words such as "believes," "intends," "may," "should," "could," "anticipates," "expected" or comparable terminology, or by discussions of strategies or trends. Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, it cannot give any assurances that these expectations will prove to be correct. Such statements by their nature involve substantial risks and uncertainties that could significantly impact expected results, and actual future results could differ materially from those described in such forward-looking statements. While it is not possible to identify all factors, the Company continues to face many risks and uncertainties. The factors that could cause actual future results to differ materially from those described herein are the risks and uncertainties discussed in this Quarterly Report and those described from time to time in the Company's other filings with the SEC include, but are not limited to, the following:

- o Future supply and demand for the Company's products,
- o The extent of the dependence of certain of the Company's businesses on certain market sectors,
- o The cyclical nature of the Company's businesses (such as Kronos' TiO2 operations),
- o Customer inventory levels (such as the extent to which Kronos' customers may, from time to time, accelerate purchases of TiO2 in advance of anticipated price increases or defer purchases of TiO2 in advance of anticipated price decreases),
- o Changes in raw material and other operating costs (such as energy and steel costs),
- o The possibility of labor disruptions,
- o General global economic and political conditions (such as changes in the level of gross domestic product in various regions of the world and the impact of such changes on demand for TiO2 and component products),
- o Demand for office furniture,
- o Competitive products and substitute products, including increased competition from low-cost manufacturing sources (such as China),
- o Customer and competitor strategies,
- o The impact of pricing and production decisions,
- o Competitive technology positions,
- o Service industry employment levels,
- o Fluctuations in currency exchange rates (such as changes in the exchange

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

- rate between the U.S. dollar and each of the euro, the Norwegian kroner, the New Taiwan dollar and the Canadian dollar),
- o Operating interruptions (including, but not limited to, labor disputes, leaks, fires, explosions, unscheduled or unplanned downtime and transportation interruptions),
 - o The ability of the Company to renew or refinance credit facilities,
 - o The ultimate outcome of income tax audits, tax settlement initiatives or other tax matters,
 - o The introduction of trade barriers,
 - o Potential difficulties in integrating completed or future acquisitions,
 - o Decisions to sell operating assets other than in the ordinary course of business,
 - o Uncertainties associated with new product development,
 - o The ultimate ability to utilize income tax attributes, the benefit of which has been recognized under the "more-likely-than-not" recognition criteria,
 - o Environmental matters (such as those requiring emission and discharge standards for existing and new facilities),
 - o Government laws and regulations and possible changes therein (such as changes in government regulations which might impose various obligations on present and former manufacturers of lead pigment and lead-based paint, including NL, with respect to asserted health concerns associated with the use of such products),
 - o The ultimate resolution of pending litigation (such as NL's lead pigment litigation and litigation surrounding environmental matters), and
 - o Possible future litigation.

Should one or more of these risks materialize (or the consequences of such a development worsen), or should the underlying assumptions prove incorrect, actual results could differ materially from those forecasted or expected. The Company disclaims any intention or obligation to update or revise any forward-looking statement whether as a result of changes in information, future events or otherwise.

Component products

	Three months ended June 30,			Six months ended June 30,		
	2004	2005	% Change	2004	2005	% Ch
	-----	-----	-----	-----	-----	-----
	(In millions, except percentages)					
Net sales	\$ 46.2	\$ 45.8	-1%	\$ 89.8	\$ 92.6	
Segment profit	5.1	4.7	-8%	7.6	8.9	+

Component product sales and operating income were lower in the second quarter of 2005 as compared to the second quarter of 2004 due primarily to the net effect of lower sales volumes partially offset by higher selling prices for certain products. Component product sales and operating income were higher in the first six months of 2005 as compared to the same period in 2004 as the effect of higher selling prices for certain products more than offset the impact of lower sales volumes for certain products. During the second quarter of 2005, sales of precision slide products were 2% higher than the second quarter of 2004, while sales of security products declined 5%. Sales of ergonomic products in the second quarter of 2005 approximated ergonomic product sales in the second quarter of 2004. For the first six months of 2005, sales of precision slide and ergonomic products increased 9% and 5%, respectively, compared to the first six months of 2004, while sales of security products declined 3%. The percentage changes in both precision slide and ergonomic products include the impact

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

resulting from changes in foreign currency exchange rates. Sales of security products are generally denominated in U.S. dollars.

CompX has substantial operations and assets located outside the United States in Canada and Taiwan. A portion of CompX's sales generated from its non-U.S. operations are denominated in currencies other than the U.S. dollar, principally the Canadian dollar and the New Taiwan dollar. In addition, a portion of CompX's sales generated from its non-U.S. operations (principally in Canada) are denominated in the U.S. dollar. Most raw materials, labor and other production costs for such non-U.S. operations are denominated primarily in local currencies. Consequently, the translated U.S. dollar values of CompX's foreign sales and operating results are subject to currency exchange rate fluctuations which may favorably or unfavorably impact reported earnings and may affect comparability of period-to-period operating results. During the first six months of 2005, currency exchange rate fluctuations did not significantly affect comparisons with 2004.

While demand has stabilized across most of CompX's product segments, certain customers continue to seek lower priced cost Asian sources as alternatives to CompX's products. CompX believes the impact of this will be mitigated through its ongoing initiatives to expand both new products and new market opportunities. Asian-sourced competitive pricing pressures are expected to continue to be a challenge. CompX's strategy in responding to the competitive pricing pressure has included reducing production cost through product reengineering, improvement in manufacturing processes or moving production to lower-cost facilities including CompX's Asian-based manufacturing facilities. CompX has also emphasized and focused on opportunities where it can provide value-added customer support services that Asian-based manufacturers are generally unable to provide. CompX believes its combination of cost control initiatives together with its value-added approach to development and marketing of products helps to mitigate the impact of pricing pressures from Asian competitors.

CompX will continue to focus on cost improvement initiatives, utilizing lean manufacturing techniques and prudent balance sheet management in order to minimize the impact of lower sales, particularly to the office furniture industry, and to develop value-added customer relationships with an additional focus on sales of CompX's higher-margin ergonomic computer support systems and security products to improve operating results. These actions, along with other activities to eliminate excess capacity, have been designed to position CompX to expand more effectively on both new product and new market opportunities to improve CompX's profitability.

Chemicals

Relative changes in Kronos' TiO2 sales and operating income during the 2004 and 2005 periods presented are primarily due to the net effects of (i) higher average TiO2 selling prices, (ii) lower TiO2 selling volumes and (iii) relative changes in foreign currency exchange rates. Selling prices (in billing currencies) for TiO2, Kronos' principal product, were generally decreasing during the first half of 2004 and increasing in the last half of 2004 and the first six months of 2005.

Three months ended June 30,			Six months e June 30	
2004	2005	% Change	2004	2005

(In millions, except percentages)

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

Net sales	\$295.8	\$311.7	+5%	\$559.1	\$603.5
Segment profit	40.1	59.2	+48%	66.3	107.2
TiO2 operating statistics:					
Sales volumes*	136	122	-10%	255	237
Production volumes*	122	127	+ 4%	240	249
Percentage change in TiO2 average selling prices:					
Using actual foreign currency exchange rates			+15%		
Impact of changes in foreign currency exchange rates			- 4%		

In billing currencies			+11%		
			====		

* Thousands of metric tons

Kronos' sales increased \$15.9 million (5%) in the second quarter of 2005 compared to the second quarter of 2004 and increased \$44.4 million (8%) in the first six months of 2005 as compared to the same period in 2004 due to the net effects of higher average TiO2 selling prices, lower TiO2 selling volumes and the favorable effect of fluctuations in foreign currency exchange rates, which increased sales by approximately \$10 million and \$21 million, respectively, as further discussed below. Excluding the effect of fluctuations in the value of the U.S. dollar relative to other currencies, Kronos' average TiO2 selling prices in billing currencies in the second quarter and first six months of 2005 were 11% higher as compared to the second quarter of 2004 and 10% higher as compared to the first six months of 2004. When translated from billing currencies to U.S. dollars using actual foreign currency exchange rates prevailing during the respective periods, Kronos' average TiO2 selling prices in the second quarter of 2005 increased 15% compared to the second quarter of 2004 and increased 14% for the first six months of 2005 compared to the first six months of 2004. Reflecting the implementation of prior price increase announcements, Kronos' average TiO2 selling prices in the second quarter of 2005 increased 2% compared to the first quarter of 2005.

Kronos' sales are denominated in various currencies, including the U.S. dollar, the euro, other major European currencies and the Canadian dollar. The disclosure of the percentage change in Kronos' average TiO2 selling prices in billing currencies (which excludes the effects of fluctuations in the value of the U.S. dollar relative to other currencies) is considered a "non-GAAP" financial measure under regulations of the SEC. The disclosure of the percentage change in Kronos' average TiO2 selling prices using actual foreign currency exchange rates prevailing during the respective periods is considered the most directly comparable financial measure presented in accordance with GAAP ("GAAP measure"). Kronos discloses percentage changes in its average TiO2 prices in billing currencies because Kronos believes such disclosure provides useful information to investors to allow them to analyze such changes without the impact of changes in foreign currency exchange rates, thereby facilitating period-to-period comparisons of the relative changes in average selling prices in the actual various billing currencies. Generally, when the U.S. dollar either strengthens or weakens against other currencies, the percentage change in average selling prices in billing currencies will be higher or lower, respectively, than such percentage changes would be using actual exchange rates prevailing during the respective periods. The difference between the 15% and 14%

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

increases in Kronos' average TiO2 selling prices during the second quarter and first six months of 2005 as compared to the second quarter and first six months of 2004 using actual foreign currency exchange rates prevailing during the respective periods (the GAAP measure), and the 11% and 10% increases in Kronos' average TiO2 selling prices in billing currencies (the non-GAAP measure) during each of such periods is due to the effect of changes in foreign currency exchange rates. The above table presents in a tabular format (i) the percentage change in Kronos' average TiO2 selling prices using actual foreign currency exchange rates prevailing during the respective periods (the GAAP measure), (ii) the percentage change in Kronos' average TiO2 selling prices in billing currencies (the non-GAAP measure) and (iii) the percentage change due to changes in foreign currency exchange rates (or the reconciling item between the non-GAAP measure and the GAAP measure).

Kronos' TiO2 sales volumes in the second quarter and first six months of 2005 decreased 10% and 7%, respectively, compared to the corresponding periods in 2004, with volumes lower in all regions of the world and with the largest decline in Europe. Kronos' income from operations comparisons were favorably impacted by higher production levels, which increased 4% in each of the second quarter and first six months of 2005 as compared to the same periods in 2004. Kronos' operating rates were near full capacity in those periods, and Kronos' production volume in the first six months of 2005 was a new record for Kronos.

Kronos' segment profit in the second quarter of 2004 includes income of \$6.3 million (\$4.1 million, or \$.08 per diluted share, net of income taxes) related to settlement of a contract dispute with a customer.

Kronos has substantial operations and assets located outside the United States (particularly in Germany, Belgium, Norway and Canada). A significant amount of Kronos' sales generated from its non-U.S. operations are denominated in currencies other than the U.S. dollar, principally the euro, other major European currencies and the Canadian dollar. A portion of Kronos' sales generated from its non-U.S. operations are denominated in the U.S. dollar. Certain raw materials, primarily titanium-containing feedstocks, are purchased in U.S. dollars, while labor and other production costs are denominated primarily in local currencies. Consequently, the translated U.S. dollar value of Kronos' foreign sales and operating results are subject to currency exchange rate fluctuations which may favorably or adversely impact reported earnings and may affect the comparability of period-to-period operating results. Overall, fluctuations in the value of the U.S. dollar relative to other currencies, primarily the euro, increased TiO2 sales by approximately a net \$10 million in the second quarter of 2005 as compared to the same period in 2004 and increased TiO2 sales in the first six months of 2005 by approximately \$21 million compared to the same period in 2004. Fluctuations in the value of the U.S. dollar relative to other currencies similarly impacted Kronos' foreign currency-denominated operating expenses. Kronos' operating costs that are not denominated in the U.S. dollar, when translated into U.S. dollars, were higher in the second quarter and first six months of 2005 as compared to the second quarter and first six months of 2004. Overall, the net impact of currency exchange rate fluctuations on Kronos' operating income comparisons resulted in approximately a net \$2 million increase and a net \$3 million increase in Kronos' income from operations in the second quarter and first six months of 2005, respectively, as compared to the corresponding periods in 2004.

Kronos expects its segment profit in 2005 will be significantly higher than 2004, due primarily to higher average selling prices. The quarterly price improvements in average selling prices since the third quarter of 2004 are the key to Kronos' anticipation that second half segment profit in 2005 will be significantly higher than the second half of 2004. Average prices in the second half of 2005 as compared to the second quarter of 2005 will likely rise modestly in North America, reflecting the expected partial implementation of prior selling price announcements. In Europe and export markets, average prices in the

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

second half of 2005 will likely decline from the second quarter of 2005. Production volumes in the second half of 2005 will likely be similar to those achieved in the second half of 2004 and are expected to be below the production volumes in the first half of 2005, due primarily to certain finishing capacity being taken temporarily offline in order to complete debottlenecking projects at Kronos' Leverkusen, Germany facility. Sales volumes in the second half of 2005 are expected to be lower than those in the second half of 2004, and are likely to be similar to the sales volumes in the first half of 2005. While Kronos expects its segment profit in calendar 2005 will be higher than calendar 2004, Kronos expects its segment profit in the second half of 2005 will be below the first half of 2005. Kronos' expectations as to the future prospects of Kronos and the TiO2 industry are based upon a number of factors beyond Kronos' control, including worldwide growth of gross domestic product, competition in the marketplace, unexpected or earlier-than-expected capacity additions and technological advances. If actual developments differ from Kronos' expectations, Kronos' results of operations could be unfavorably affected.

Kronos' efforts to debottleneck its production facilities to meet long-term demand continue to prove successful. Such debottlenecking efforts included, among other things, the addition of back-end finishing capacity to be able to process a larger quantity of the base TiO2 produced and equipment upgrades and enhancements to allow for reduced downtime for maintenance activities. Kronos' production capacity has increased by approximately 30% over the past ten years due to debottlenecking programs, with only moderate capital expenditures. Kronos believes its annual attainable production capacity for 2005 is approximately 500,000 metric tons, with approximately 10,000 metric tons additional capacity available in 2006 through its continued debottlenecking efforts.

Equity in earnings of Kronos - 2005

	Three months ended June 30, 2005	Six months ended June 30, 2005
	-----	-----
	(In millions)	
Kronos historical:		
Net sales	\$ 311.7	\$ 603.5
Segment profit	59.2	107.2
Security transaction gain	5.4	5.4
Other general corporate, net	(1.1)	(2.2)
Interest expense	(11.6)	(23.4)
	-----	-----
Income tax expense	51.9	87.0
	19.0	32.7
Net income	\$ 32.9	\$ 54.3
Equity in earnings of Kronos Worldwide, Inc.	\$ 11.8	\$ 19.6

See the preceding discussion relating to Kronos' segment profit for the second quarter and first six months of 2005. The security transaction gain in the second quarter of 2005 relates to Kronos' sale of its passive interest in a Norwegian smelting operation, which had a nominal carrying value for financial reporting purposes, for approximately \$5.4 million (\$1.3 million or \$.03 per diluted share, net of income taxes and minority interest to the Company). Kronos' interest expense in the second quarter and first six months of 2005

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

relates principally to Kronos International, Inc.'s ("KII") Senior Secured Notes.

General corporate items

Securities transactions. Securities transactions in the second quarter and first six months of 2005 relate principally to a \$14.7 million pre-tax gain (\$8.0 million, or \$.17 per diluted share, net of income taxes) related to NL's sale of approximately 470,000 shares of Kronos common stock in market transactions during the six months ended June 30, 2005. See Note 2 to the Consolidated Financial Statements.

Interest expense. Substantially all of the interest expense in the second quarter and first six months of 2004 relates to Kronos. Interest expense related to CompX declined by approximately \$100,000 and \$200,000 in the second quarter and first six months of 2005, respectively compared to the corresponding periods in 2004 due primarily to lower average levels of outstanding debt. CompX expects interest expense will continue to be lower during the remainder of 2005 as compared to the last half of 2004 due to lower average levels of outstanding debt.

Insurance recoveries. NL has reached an agreement with one of its former insurance carriers in which such carrier would reimburse NL for a portion of its past and future lead pigment litigation defense costs, although the amount which NL will ultimately recover from such carrier with respect to such defense costs incurred by NL is not yet determinable. NL is also continuing discussions with another former insurance carrier with respect to recovery of past and future defense costs. In addition, during the second quarter of 2005, NL recognized \$1.2 million of expected recoveries from certain insolvent former insurance carriers relating to settlement of excess insurance coverage claims. See Note 11 to the Consolidated Financial Statements. While NL continues to seek additional recoveries of past defense costs as well as an agreement related to future defense costs, there can be no assurance that NL will be successful in obtaining reimbursement for either defense costs or indemnity. NL has not considered any potential insurance recoveries in determining related accruals for lead pigment litigation matters. Any such additional insurance recoveries would be recognized when their receipt is deemed probable and the amount is determinable.

General corporate expenses. Net general corporate expenses in the second quarter and first six months of 2005 were lower than the same periods of 2004 due primarily to lower environmental remediation and legal expenses of NL. Net general corporate expenses in calendar 2005 are currently expected to be higher than 2004, primarily due to higher expected legal expenses of NL resulting from an increase in litigation and related expenses for the remainder of 2005. However, obligations for environmental remediation are difficult to assess and estimate and no assurance can be given that actual costs will not exceed accrued amounts or that costs will not be incurred with respect to sites for which no estimate of liability can presently be made. See Note 14 to the Consolidated Financial Statements.

Provision for income taxes

The principal reasons for the difference between the Company's effective income tax rate and the U.S. federal statutory income tax rates are explained in Note 12 to the Consolidated Financial Statements. As discussed in Note 1 to the Consolidated Financial Statements, the Company's consolidated financial statements have been restated, including significant changes in the Company's previously-reported provision for income taxes.

As previously reported, the Company's income tax benefit in the second quarter of 2004 includes (i) a \$268.6 million income tax benefit (\$135.7

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

million, or \$2.80 per diluted share, net of minority interest) related to the reversal of a deferred income tax asset valuation allowance attributable to Kronos' income tax attributes in Germany (principally net operating loss carryforwards) and (ii) a \$49.1 million income tax benefit (\$1.00 per diluted share) related to income tax attributes of a subsidiary of NL.

As previously disclosed, the Company commenced to recognize deferred income taxes with respect to the excess of the financial reporting carrying amount over the income tax basis of its investment in Kronos beginning in December 2003 following the Company's pro-rata distribution of shares of Kronos common stock to NL's shareholders. The aggregate amount of such deferred income taxes included in the Company's provision for income taxes was \$47.7 million in the six months ended June 30, 2004 and \$984,000 in the six months ended June 30, 2005. In addition, the Company's provision for income taxes in the six months ended June 30, 2004 and 2005 includes an aggregate \$387,000 and \$913,000, respectively, for the current income tax effect related to NL's distribution of such shares of Kronos common stock to its shareholders.

Minority interest

See Note 10 to the Consolidated Financial Statements.

Discontinued operations.

See Note 15 to the Consolidated Financial Statements.

Accounting principles not yet implemented.

See Note 16 to the Consolidated Financial Statements.

LIQUIDITY AND CAPITAL RESOURCES:

Consolidated cash flows

Summary

The Company's primary source of liquidity on an ongoing short-term (defined as the twelve-month period ending June 30, 2006) and long-term (defined as the five-year period ending December 31, 2009, the time period for which the Company generally does long-term budgeting) basis is its cash flows from operating activities, which is generally used to (i) fund capital expenditures, (ii) repay any short-term indebtedness incurred primarily for working capital purposes and (iii) provide for the payment of dividends. In addition, from time-to-time the Company may incur indebtedness, generally to (i) fund short-term working capital needs, (ii) refinance existing indebtedness or (iii) fund major capital expenditures or the acquisition of other assets outside the ordinary course of business. Also, the Company may from time-to-time sell assets outside the ordinary course of business, the proceeds of which are generally used to (i) repay existing indebtedness (including indebtedness which may have been collateralized by the assets sold), (ii) make investments in marketable and other securities, (iii) fund major capital expenditures or the acquisition of other assets outside the ordinary course of business or (iv) pay dividends.

Operating activities

Cash flows from operating activities decreased from \$71.6 million provided by operating activities in the first six months of 2004 to \$18.1 million of cash used by operating activities in the first six months of 2005. This \$89.7 million decrease was due primarily to the deconsolidation of Kronos, effective July 1,

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

2004. As such, cash from operating activities in the first six months of 2005 is not comparable to the corresponding period in 2004. Relative changes in accounts receivable are affected by, among other things, the timing of sales and the collection of the resulting receivables. Relative changes in inventories and accounts payable and accrued liabilities are affected by, among other things, the timing of raw material purchases and the payment for such purchases and the relative difference between production volumes and sales volumes. Relative changes in accrued environmental costs are affected by, among other things, the period in which recognition of the environmental accrual is recognized and the period in which the remediation expenditure is actually made.

Trends in cash flows from operating activities (excluding the impact of significant asset dispositions and relative changes in assets and liabilities) are generally similar to trends in the Company's earnings. However, certain items included in the determination of net income are non-cash, and therefore such items have no impact on cash flows from operating activities. Non-cash items included in the determination of net income include depreciation and amortization expense, deferred income taxes and non-cash interest expense. Non-cash interest expense relates principally to Kronos in 2004 and consists of amortization of original issue discount or premium on certain indebtedness and amortization of deferred financing costs.

Certain other items included in the determination of net income may have an impact on cash flows from operating activities, but the impact of such items on cash flows from operating activities will differ from their impact on net income. For example, equity in earnings of affiliates will generally differ from the amount of distributions received from such affiliates, and equity in losses of affiliates does not necessarily result in current cash outlays paid to such affiliates. The amount of periodic defined benefit pension plan expense and periodic OPEB expense depends upon a number of factors, including certain actuarial assumptions, and changes in such actuarial assumptions will result in a change in the reported expense. In addition, the amount of such periodic expense generally differs from the outflows of cash required to be currently paid for such benefits.

Certain other items included in the determination of net income have no impact on cash flows from operating activities, but such items do impact cash flows from investing activities (although their impact on such cash flows differs from their impact on net income). For example, realized gains and losses from the disposal of long-lived assets are included in the determination of net income, although the proceeds from any such disposal are shown as part of cash flows from investing activities.

Relative changes in working capital assets and liabilities can have a significant effect on cash flows from operating activities. CompX's average days sales outstanding related to its continuing operations increased from 38 days at December 31, 2004 to 42 days at June 30, 2005, due to the timing of collection on the slightly higher accounts receivable balance at the end of June. CompX's average number of days in inventory related to its continuing operations was 52 days at both December 31, 2004 and June 30, 2005.

Relative changes in assets and liabilities generally result from the timing of production, sales, purchases and income tax payments. Such relative changes can significantly impact the comparability of cash flow from operations from period to period, as the income statement impact of such items may occur in a different period from when the underlying cash transaction occurs. For example, raw materials may be purchased in one period, but the payment for such raw materials may occur in a subsequent period. Similarly, inventory may be sold in one period, but the cash collection of the receivable may occur in a subsequent period.

NL does not have complete access to the cash flows of its subsidiaries and

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

affiliates, in part due to limitations contained in certain credit agreements as well as the fact that certain of such subsidiaries and affiliates are not 100% owned by NL. A detail of NL's consolidated cash flows from operating activities is presented in the table below. Eliminations consist of intercompany dividends (most of which are paid by Kronos to NL in 2004, and by CompX to NL in 2005).

	Six months ended June 30,	
	2004	2005
	-----	-----
	(In millions)	
Cash provided (used) by operating activities:		
Kronos	\$ 67.5	\$ -
CompX	13.6	8.7
NL Parent	3.8	(7.9)
Other	(.9)	(16.3)
Eliminations	(12.4)	(2.6)
	-----	-----
	\$ 71.6	\$ (18.1)
	=====	=====

Investing and financing activities

In 2005, substantially all of the Company's consolidated capital expenditures relate to CompX. During the first six months of 2005, (i) NL sold shares of Kronos common stock in market transactions for \$19.2 million, (ii) CompX received a net \$18.1 million from the sale of its Thomas Regout operations (which had approximately \$4.0 million of cash at the date of disposal), (iii) NL acquired CompX common stock in market transactions for \$572,000 and (iv) NL collected \$2 million on its loan to one of the Contran family trusts. See Notes 2 and 15 to the Consolidated Financial Statements.

Distributions to minority interest in 2005 consist of CompX dividends paid to shareholders other than NL. Other cash flows from financing activities in 2005 relate primarily to proceeds from the issuance of NL and CompX common stock upon exercise of stock options.

At June 30, 2005, unused credit available under existing credit facilities approximated \$47.5 million, all under CompX's revolving credit facility.

Provisions contained in certain of the Company's and its subsidiaries' and affiliates' credit agreements could result in the acceleration of the applicable indebtedness prior to its stated maturity for reasons other than defaults from failing to comply with typical financial covenants. For example, certain credit agreements allow the lender to accelerate the maturity of the indebtedness upon a change of control (as defined) of the borrower. In addition, certain credit agreements could result in the acceleration of all or a portion of the indebtedness following a sale of assets outside the ordinary course of business, which provision was waived in connection with CompX's sale of its Thomas Regout operations. Other than operating leases discussed in the 2004 Annual Report, neither NL nor any of its subsidiaries or affiliates are parties to any off-balance sheet financing arrangements.

Component products - CompX

CompX received approximately \$18.1 million cash (net of expenses) in

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

January 2005 upon the sale of its Thomas Regout operations in the Netherlands. See Note 15 to the Consolidated Financial Statements. CompX believes that its cash on hand, together with cash generated from operations and borrowing availability under its bank credit facility, will be sufficient to meet CompX's liquidity needs for working capital, capital expenditures and dividends. To the extent that CompX's actual operating results or developments differ from CompX's expectations, CompX's liquidity could be adversely affected. CompX, which had suspended its regular quarterly dividend of \$.125 per share in the second quarter of 2003, reinstated its regular quarterly dividend at the \$.125 per share rate in the fourth quarter of 2004.

Certain of the CompX's sales generated by its non-U.S. operations are denominated in U.S. dollars. CompX periodically uses currency forward contracts to manage a very nominal portion of foreign exchange rate risk associated with receivables denominated in a currency other than the holder's functional currency or similar exchange rate risk associated with future sales. CompX has not entered into these contracts for trading or speculative purposes in the past, nor does CompX currently anticipate entering into such contracts for trading or speculative purposes in the future. Derivatives used to hedge forecasted transactions and specific cash flows associated with foreign currency denominated financial assets and liabilities which meet the criteria for hedge accounting are designated as cash flow hedges. Consequently, the effective portion of gains and losses is deferred as a component of accumulated other comprehensive income and is recognized in earnings at the time the hedged item affects earnings. Contracts that do not meet the criteria for hedge accounting are marked-to-market at each balance sheet date with any resulting gain or loss recognized in income currently as part of net currency transactions. To manage such exchange rate risk, at June 30, 2005, CompX held a series of contracts maturing through September 2005, to exchange an aggregate of U.S. \$6.5 million for an equivalent amount of Canadian dollars at an exchange rates of Cdn. \$1.25 to Cdn. \$1.26 per U.S. dollar. At June 30, 2005, the actual exchange rate was Cdn. \$1.23 per U.S. dollar. The estimated fair values of such foreign currency forward contracts at June 30, 2005 is not material.

CompX periodically evaluates its liquidity requirements, alternative uses of capital, capital needs and available resources in view of, among other things, its capital expenditure requirements, dividend policy and estimated future operating cash flows. As a result of this process, CompX has in the past and may in the future seek to raise additional capital, refinance or restructure indebtedness, issue additional securities, modify its dividend policy, repurchase shares of its common stock or take a combination of such steps or other steps to manage its liquidity and capital resources. In the normal course of business, CompX may review opportunities for acquisitions, divestitures, joint ventures or other business combinations in the component products industry. In the event of any such transaction, CompX may consider using cash, issuing additional equity securities or increasing the indebtedness of CompX or its subsidiaries.

Chemicals - Kronos

At June 30, 2005, Kronos had cash, cash equivalents and marketable debt securities of \$21.2 million, including restricted balances of \$3.6 million, and Kronos had approximately \$155 million available for borrowing under its U.S., Canadian and European credit facilities. Based upon Kronos' expectations for the TiO₂ industry and anticipated demands on Kronos' cash resources as discussed herein, Kronos expects to have sufficient liquidity to meet its future obligations including operations, capital expenditures, debt service and current dividend policy. To the extent that actual developments differ from Kronos' expectations, Kronos' liquidity could be adversely affected.

At June 30, 2005, Kronos' outstanding debt was comprised of (i) \$461.1 million related to KII's Senior Secured Notes and (ii) approximately \$200,000 of

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

other indebtedness. During the second quarter of 2005, Kronos extended the respective maturity dates of its European and U.S. revolving credit facilities, each by three years to June 2008 and September 2008, respectively.

Kronos' assets consist primarily of investments in its operating subsidiaries, and Kronos' ability to service its parent level obligations, including the Senior Secured Notes, depends in large part upon the distribution of earnings of its subsidiaries, whether in the form of dividends, advances or payments on account of intercompany obligation, or otherwise. None of Kronos' subsidiaries have guaranteed the Senior Secured Notes, although KII has pledged 65% of the common stock or other ownership interest of certain of KII's first-tier operating subsidiaries as collateral of such Senior Secured Notes.

Pricing within the TiO2 industry is cyclical, and changes in industry economic conditions significantly impact Kronos' earnings and operating cash flows. Cash flows from operations is considered the primary source of liquidity for Kronos. Changes in TiO2 pricing, production volumes and customer demand, among other things, could significantly affect the liquidity of Kronos.

Based upon Kronos' expectations for the TiO2 industry and anticipated demand for Kronos' cash resources as discussed herein, Kronos expects to have sufficient short-term and long-term liquidity to meet its obligations including operations, capital expenditures, debt service and dividends. To the extent that actual developments differ from Kronos' expectations, Kronos' liquidity could be adversely affected.

See Note 12 to the Consolidated Financial Statements for certain income tax examinations currently underway with respect to certain of Kronos' income tax returns in various non-U.S. jurisdictions, and see Note 14 to the Consolidated Financial Statements with respect to certain legal proceedings with respect to Kronos.

Certain of the Kronos' sales generated by its non-U.S. operations are denominated in U.S. dollars. Kronos periodically uses currency forward contracts to manage a very nominal portion of foreign exchange rate risk associated with receivables denominated in a currency other than the holder's functional currency or similar exchange rate risk associated with future sales. Kronos has not entered into these contracts for trading or speculative purposes in the past, nor does Kronos currently anticipate entering into such contracts for trading or speculative purposes in the future. Derivatives used to hedge forecasted transactions and specific cash flows associated with foreign currency denominated financial assets and liabilities which meet the criteria for hedge accounting are designated as cash flow hedges. Consequently, the effective portion of gains and losses is deferred as a component of accumulated other comprehensive income and is recognized in earnings at the time the hedged item affects earnings. Contracts that do not meet the criteria for hedge accounting are marked-to-market at each balance sheet date with any resulting gain or loss recognized in income currently as part of net currency transactions. For the periods ended June 30, 2004 and 2005, Kronos has not used hedge accounting for any of its contracts. To manage such exchange rate risk, at June 30, 2005, Kronos held a series of contracts, which mature through December 2005, to exchange an aggregate of U.S. \$22.5 million for an equivalent amount of Canadian dollars at an exchange rate of Cdn. \$1.23 to Cdn. \$1.26 per U.S. dollar. At June 30, 2005, the actual exchange rate was Cdn. \$1.23 per U.S. dollar. The estimated fair value of such foreign currency forward contracts at June 30, 2005 was not material.

Kronos International's assets consist primarily of investments in its operating subsidiaries, and its ability to service its parent level obligations, including the Senior Secured Notes, depends in large part upon the distribution of earnings of its subsidiaries, whether in the form of dividends, advances or payments on account of intercompany obligation, or otherwise. None of its

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

subsidiaries have guaranteed the Senior Secured Notes, although Kronos International has pledged 65% of the common stock or other ownership interest of certain of its first-tier operating subsidiaries as collateral of such Senior Secured Notes.

Kronos periodically evaluates its liquidity requirements, alternative uses of capital, capital needs and availability of resources in view of, among other things, its dividend policy, its debt service and capital expenditure requirements and estimated future operating cash flows. As a result of this process, Kronos has in the past and may in the future seek to reduce, refinance, repurchase or restructure indebtedness, raise additional capital, repurchase shares of its common stock, modify its dividend policy, restructure ownership interests, sell interests in subsidiaries or other assets, or take a combination of such steps or other steps to manage its liquidity and capital resources. In the normal course of its business, Kronos may review opportunities for the acquisition, divestiture, joint venture or other business combinations in the chemicals or other industries, as well as the acquisition of interests in, and loans to, related entities. In the event of any such transaction, Kronos may consider using available cash, issuing equity securities or increasing indebtedness to the extent permitted by the agreements governing Kronos' existing debt.

Kronos has substantial operations located outside the United States for which the functional currency is not the U.S. dollar. As a result, the reported amounts of Kronos' assets and liabilities related to its non-U.S. operations, and therefore Kronos' net assets, will fluctuate based upon changes in currency exchange rates.

NL Industries

At June 30, 2005, NL (exclusive of CompX) had cash, cash equivalents and marketable debt securities of \$84.3 million, including restricted balances of \$16.2 million. Of such restricted balances, \$2.8 million was held by special purpose trusts, the assets of which can only be used to pay for certain of NL's future environmental remediation and other environmental expenditures. See Note 14 to the Consolidated Financial Statements.

See Note 12 to the Consolidated Financial Statements for certain income tax examinations currently underway with respect to certain of NL's income tax returns, and see Note 14 to the Consolidated Financial Statements and Part II, Item 1, "Legal Proceedings" with respect to certain legal proceedings and environmental matters with respect to NL.

In addition to those legal proceedings described in Note 14 to the Consolidated Financial Statements, various legislation and administrative regulations have, from time to time, been proposed that seek to (i) impose various obligations on present and former manufacturers of lead pigment and lead-based paint with respect to asserted health concerns associated with the use of such products and (ii) effectively overturn court decisions in which NL and other pigment manufacturers have been successful. Examples of such proposed legislation include bills which would permit civil liability for damages on the basis of market share, rather than requiring plaintiffs to prove that the defendant's product caused the alleged damage, and bills which would revive actions barred by the statute of limitations. While no legislation or regulations have been enacted to date that are expected to have a material adverse effect on NL's consolidated financial position, results of operations or liquidity, enactment of such legislation could have such an effect.

NL periodically evaluates its liquidity requirements, alternative uses of capital, capital needs and availability of resources in view of, among other things, its dividend policy and capital expenditure requirements and estimated future operating cash flows. As a result of this process, NL has in the past and

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

may in the future seek to reduce, refinance, repurchase or restructure indebtedness, raise additional capital, repurchase shares of its common stock, modify its dividend policy, restructure ownership interests, sell interests in subsidiaries or other assets, or take a combination of such steps or other steps to manage its liquidity and capital resources. In the normal course of its business, NL may review opportunities for the acquisition, divestiture, joint venture or other business combinations in the chemicals or other industries, as well as the acquisition of interests in, and loans to, related entities.

Because NL's operations are conducted primarily through its subsidiaries and affiliates, NL's long-term ability to meet its parent company level corporate obligations is dependent in large measure on the receipt of dividends or other distributions from its subsidiaries and affiliates. In the fourth quarter of 2004, CompX reinstated its regular quarterly dividend at the \$.125 per share rate. At that rate, and based on the 10.4 million shares of CompX held directly or indirectly by NL at June 30, 2005, NL would receive aggregate annual dividends from CompX of \$5.2 million. Kronos' current quarterly dividend is \$.25 per share. At that rate, and based on the 17.5 million shares of Kronos held by NL at June 30, 2005, NL would receive aggregate annual dividends from Kronos of \$17.5 million.

The Company and related entities routinely evaluate acquisitions of interests in, or combinations with, companies, including related companies, perceived by management to be undervalued in the marketplace. These companies may or may not be engaged in businesses related to the Company's current businesses. The Company intends to consider such acquisition activities in the future and, in connection with this activity, may consider issuing additional equity securities and increasing the indebtedness of the Company, its subsidiaries and related companies. From time to time, the Company and related entities also evaluate the restructuring of ownership interests among their respective subsidiaries and related companies.

Non-GAAP financial measures

In an effort to provide investors with additional information regarding the Company's results of operations as determined by GAAP, the Company has disclosed certain non-GAAP information which the Company believes provides useful information to investors.

- o The Company discloses percentage changes in Kronos' average TiO₂ selling prices in billing currencies, which excludes the effects of foreign currency translation. The Company believes disclosure of such percentage changes allows investors to analyze such changes without the impact of changes in foreign currency exchange rates, thereby facilitating period-to-period comparisons of the relative changes in average selling prices in the actual various billing currencies. Generally, when the U.S. dollar either strengthens or weakens against other currencies, the percentage change in average selling prices in billing currencies will be higher or lower, respectively, than such percentage changes would be using actual exchange rates prevailing during the respective periods.

ITEM 4. CONTROLS AND PROCEDURES

Restatement. As disclosed in Note 1 to the Consolidated Financial Statements, the Company and its audit committee concluded to restate the Company's consolidated financial statements as of December 31, 2004 and June 30, 2005, and for the interim periods ended June 30, 2004 and 2005. The restatement relates to misstatements of the Company's provision for income taxes for the interim periods ended June 30, 2004 and 2005, and the Company's related income tax accounts (current and deferred) as of December 31, 2004 and June 30, 2005.

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

The guidance set forth in Auditing Standard No. 2 of the Public Company Accounting Oversight Board states that a restatement of previously-issued financial statements to reflect the correction of a misstatement should be regarded as at least a significant control deficiency and as a strong indicator that a material weakness in internal control over financial reporting exists. As a result of this restatement, the Company has concluded that a material weakness existed at December 31, 2004 and June 30, 2005.

Evaluation of Disclosure Controls and Procedures. The Company maintains a system of disclosure controls and procedures. The term "disclosure controls and procedures," as defined by regulations of the SEC, means controls and other procedures that are designed to ensure that information required to be disclosed in the reports that the Company files or submits to the SEC under the Securities Exchange Act of 1934, as amended (the "Act"), is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files or submits to the SEC under the Act is accumulated and communicated to the Company's management, including its principal executive officer and its principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions to be made regarding required disclosure. Each of Harold C. Simmons, the Company's President and Chief Executive Officer, and Gregory M. Swalwell, the Company's Vice President and Chief Financial Officer, have evaluated the Company's disclosure controls and procedures as of June 30, 2005. Based upon their evaluation, and as a result of the material weakness discussed below, these executive officers have concluded that the Company's disclosure controls and procedures are not effective as of the date of such evaluation.

A material weakness is a control deficiency, or a combination of control deficiencies, that results in a more than remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. As of June 30, 2005, the Company did not maintain effective controls over the accounting for income taxes, including the determination and reporting of income taxes payable to affiliates, deferred income tax assets and liabilities, deferred income tax asset valuation allowance, and the provision for income taxes which contributed to the following material weaknesses:

- a) The Company did not have effective controls over the proper consideration of the effect of subsequent events on the evaluation of certain income tax attributes and related deferred income tax asset valuation allowances in the preparation of its consolidated financial statements in accordance with accounting principles generally accepted in the United States of America. Specifically, the Company did not have effective controls in place to consider that as a result of the capital gains generated from the Company's first quarter 2005 sales of certain securities that the Company should not have recognized a valuation allowance against certain deferred income tax assets as of December 31, 2004. This control deficiency resulted in the restatement of the 2004 Company's consolidated financial statements as of and for the year ended December 31, 2004 included in the Original Form 10-K. Additionally, this control deficiency could result in a misstatement of deferred income tax assets and liabilities and the related income tax provision that would result in a material misstatement to the Company's annual or interim consolidated financial statements that would not be prevented or detected.
- b) The Company did not have adequate personnel with sufficient knowledge of accounting principles generally accepted in the United States of America related to income tax accounting and reporting. Additionally, the Company did not maintain effective controls over the review and monitoring of the accuracy, completeness and valuation of the components of the income tax

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

provision and related deferred income taxes, and income taxes payable resulting in errors in (i) the accounting for the income tax effect of the difference between book and income tax basis of the Company's investment in Kronos Worldwide, Inc., an equity-method investment of the Company as of December 31, 2004, (ii) current and deferred income taxes related to the Company's distributions of Kronos common stock to the Company's stockholders and (iii) current and deferred income taxes related to other items, that were not prevented or detected. This control deficiency resulted in the restatement of the Company's 2002, 2003 and 2004 consolidated financial statements and 2004 and 2005 interim financial information. Additionally, this control deficiency could result in a misstatement of income taxes payable, deferred income tax assets and liabilities, deferred income tax asset valuation allowance, and the provision for income taxes that would result in a material misstatement to the Company's annual or interim consolidated financial statements that would not be prevented or detected.

Accordingly, management of the Company determined that each of these control deficiencies constitutes a material weakness.

Remediation. In order to remediate this material weakness, the Company intends to increase its financial reporting staff, with particular emphasis on obtaining additional personnel with a background in the financial reporting requirements for the determination of the provision for income taxes in accordance with SFAS No. 109 and related GAAP. Such additional staff could be employees of the Company and/or independent contractors hired by the Company with qualifications in the required area. As of December 23, 2005, two such persons have been hired. Management believes that the addition of such staff with these qualifications will help ensure that GAAP has been appropriately and consistently applied with respect to the accurate calculation and classification within the consolidated financial statements of income tax provisions and related current and deferred income tax accounts.

Changes in Internal Control Over Financial Reporting. There has been no change to the Company's internal control over financial reporting during the quarter ended June 30, 2005 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Reference is made to Note 14 to the Consolidated Financial Statements and to the 2004 Annual Report for descriptions of certain previously reported legal proceedings.

Thomas v. Lead Industries Association, et al. (Circuit Court, Milwaukee, Wisconsin, Case No. 99-CV-6411). In July 2005, the Wisconsin Supreme Court affirmed the appellate court's dismissal of plaintiff's civil conspiracy and enterprise liability claims and reversed and remanded the appellate court's dismissal of plaintiff's risk contribution claim.

State of Rhode Island v. Lead Industries Association, et al. (Superior Court of Rhode Island, No. 99-5226). In June 2005, NL filed a motion for summary

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

judgment on the state's Unfair Trade Practices Act claim.

Barker, et al. v. The Sherwin-Williams Company, et al. (Circuit Court of Jefferson County, Mississippi, Civil Action No. 2000-587, and formerly known as Borden, et al. vs. The Sherwin-Williams Company, et al.). With respect to the eight plaintiffs remaining in Holmes County Mississippi, three of these plaintiffs voluntarily dismissed their claims without prejudice in May 2005. With respect to the two plaintiffs remaining in Jefferson County, one of these plaintiffs voluntarily dismissed his claim without prejudice in May 2005.

City of Milwaukee v. NL Industries, Inc. and Mautz Paint (Circuit Court, Civil Division, Milwaukee County, Wisconsin, Case No. 01CV003066). In July 2005, NL withdrew its petition to the Wisconsin Supreme Court seeking review of the appellate court's ruling in December 2004 that reversed and remanded the trial court's dismissal of the case.

Jackson, et al., v. Phillips Building Supply of Laurel, et al. (Circuit Court of Jones County, Mississippi, Dkt. Co. 2002-10-CV1). In May 2005, the court set a trial date of November 2006.

Harris County, Texas v. Lead Industries Association, et al. (District Court of Harris County, Texas, No. 2001-21413). In May 2005, the plaintiff voluntarily dismissed the case without prejudice.

City of Chicago vs. American Cyanamid, et al. (Circuit Court of Cook County, Illinois, No. 02CH16212). In May 2005, the Illinois Supreme Court denied plaintiff's petition seeking review of the appellate court's decision affirming the dismissal of the case.

Russell v. NL Industries, Inc., et al. (Circuit Court of LeFlore County, Mississippi, Civil Action No. No.2002-0235-CICI). In May 2005, the court dismissed the case with prejudice.

Item 4. Submission of Matters to a Vote of Security Holders

The Company's 2005 Annual Meeting of Shareholders was held on May 19, 2005. Cecil H. Moore, Jr., Glenn R. Simmons, Harold C. Simmons, Thomas P. Stafford, Steven L. Watson and Terry N. Worrell were elected as directors, each receiving votes "For" their election from at least 93.4% of the 48.5 million common shares eligible to vote at the Annual Meeting.

Item 6. Exhibits

31.1 - Certification

31.2 - Certification

32.1 - Certification

The Company has retained a signed original of any of the above exhibits that contains signatures, and the Company will provide such exhibit to the Commission or its staff upon request. NL will also furnish, without charge, a copy of its Code of Business Conduct and Ethics, its Audit Committee Charter and its Corporate Governance Guidelines, each as adopted by the Company's board of directors, upon request. Such requests should be directed to the attention of NL's Corporate Secretary at NL's corporate offices located at 5430 LBJ Freeway, Suite 1700, Dallas, Texas 75240.

SIGNATURES

Edgar Filing: NL INDUSTRIES INC - Form 10-Q/A

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

NL INDUSTRIES, INC.

(Registrant)

Date December 22, 2005

By /s/ Gregory M. Swalwell

Gregory M. Swalwell
Vice President,
Finance and Chief Financial
Officer (Principal
Financial Officer)

Date December 22, 2005

By /s/ James W. Brown

James W. Brown
Vice President and Controller
(Principal Accounting Officer)