KEITH COMPANIES INC
Form 10-K
March 10, 2004

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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

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

For the fiscal year ended December 31, 2003

Commission File Number 0-26561

The Keith Companies, Inc.

(Exact name of registrant as specified in its charter)

California	**33-0203193**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

19 Technology Drive, Irvine, California 92618

(Address of principal executive offices and zip code)

Registrant s telephone number, including area code:

(949) 923-6001

Securities registered pursuant to Section 12(b) of the Act:

None

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.001 par value

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. þ

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

The number of outstanding shares of the registrant s common stock as of February 6, 2004 was 7,673,720 shares. Based on the closing sale price on the NASDAQ National Market on June 30, 2003, the aggregate market value of the registrant s common stock held by non-affiliates was approximately $63,000,000.[1]

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates certain information by reference from the registrant s definitive proxy statement for the Annual Meeting of Shareholders scheduled to be held on May 18, 2004.

[1] For purposes of this calculation, shares owned by executive officers and directors have been deemed to be owned by affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

THE KEITH COMPANIES, INC.

ANNUAL REPORT ON FORM 10-K

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PART I

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains certain forward-looking statements, including and/or concerning among others:

forecasts of earnings, revenue or other financial items;

anticipated growth in the real estate development and public works/infrastructure industry and the energy/industrial industry;

our business strategy for expanding our presence in these industries;

anticipated growth and economic expansion in the Western and Midwestern United States;

anticipated trends in our financial condition and results of operations;

anticipated growth in the pace and size of our acquisitions;

anticipated impact of future acquisitions on the condition of our business by industry and geographic location;

the long-term nature of our projects;

our ability to attract and retain employees;

our business strategy for integrating businesses that we acquire;

our ability to sustain our growth and profitability; and

our ability to distinguish ourselves from our current and future competitors.

We generally identify forward-looking statements in this Report using words like believe, expect, estimate, may, plan, should plan, contemplate, anticipate, predict or similar expressions. You may find some of these statements under Management s Discussion and Analysis of Financial Condition and Results of Operations, and Business and elsewhere is this Report. These statements involve known and unknown risks, uncertainties and other factors, including those described in the Risk Factors section, that may cause our or our industry s actual results, levels of activity, performance or achievements to differ from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Except as required by applicable law, including the securities laws of the United States, and the rules and regulations of the Securities and Exchange Commission, we do not plan to publicly update or revise any forward-looking statements after we file this Report, whether as a result of any new information, future events or otherwise.

Item 1. *Business*

General

We are a full service engineering and consulting services firm providing professional services on a wide range of projects to the real estate development and public works/infrastructure industry, and to the energy/industrial industry. We benefit from a diverse public and private client base including real estate developers, residential and commercial builders, architects, cities, counties, water districts, state and federal agencies, land owners, commercial retailers, energy providers and various manufacturers. Our professional staff and project workers provide a comprehensive menu of services that are needed to effectively manage, engineer and design infrastructure and state-of-the-art facilities.

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The following illustrates the range of services that we offer:

From 1999 through 2003, our net revenue has grown by a compounded annual growth rate of 23% and our net income from continuing operations has grown at a compounded annual growth rate of 38%. We have accomplished this through both our acquisition strategy to diversify the scope of our services and our geographic presence and through internal growth. We have acquired eight companies since December 1, 1997 and as of March 1, 2004 operate from 14 primary divisions in 7 states: California, Nevada, Utah, Arizona, Oregon, Texas and Michigan. In addition, we also have small operating activities in Brazil.

Industries Served

We serve the real estate development and public works/infrastructure industry, and the energy/industrial industry.

Real Estate Development and Public Works/ Infrastructure

Real Estate Development

Residential, commercial, golf, and other recreational developers use technical consultants to provide planning and environmental services to create land use plans, write the supporting planning and environmental documents and process entitlements and permits through governmental authorities. Technical consultants also assist clients with obtaining approvals and permits from federal, state and local agencies. After projects are approved by governmental agencies, developers need surveying, mapping, and civil engineering services to survey development sites, create accurate boundary and base maps, and provide engineering designs for grading, streets, sewer and water pipelines and facilities, utilities and drainage facilities. Upon completion of the design phase, surveyors provide construction staking services to identify the precise locations of streets, utilities, pipelines, and other facilities. In culturally sensitive areas, developers may also require environmental

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and archaeology services for planning and assistance with environmental approvals as well as construction and post-construction phase monitoring services.

Residential development includes large-scale communities, senior citizen and retirement communities, single family homes, condominiums and apartments. Commercial development includes the development and construction of retail, office, hotel and industrial facilities. Golf and recreational facility development includes golf courses, driving ranges, parks, clubhouses, theme parks, resorts and lakes.

There are generally two types of real estate development clients: the land developer and the builder. Some take on characteristics of both. Developers generally must look long-term, utilize longer-term investment financing and evaluate the performance of projects across multiple business cycles. The developer pursues land development rights and implements the process of designing and constructing infrastructure utility, roadway and landform grading improvements. A developer s projects often span several years or even decades. The builder, on the other hand, generally provides an end-user product, including homes, retail stores, restaurants or clubhouses. The builder s approach is generally based upon current and relatively short-term economic conditions. Financing for a builder s work is often construction-oriented and anticipates short-term returns. The builder often buys property that has already been zoned, graded and otherwise improved by the land developer.

Public Works/ Infrastructure

Water resources, transportation, and other public works projects provide ongoing, more reliable sources of revenue for engineering firms and consultants than private real estate development activities which may decline during unfavorable economic periods. These public projects are often long-term and have historically provided more determinable and consistent revenue streams than non-publicly funded projects. In the last couple of years, the public works/infrastructure industry segment has shown a high interest in assessing the security of these facilities in addition to enhancing the quality and availability of them.

Water Resources. Water resource services encompass the study and analysis of rainfall, water collection and distribution, use of water for cleanliness, nourishment and irrigation and the treatment and disposal of used or contaminated water. Due to the multiple demands for municipal, environmental and agricultural uses, water is a resource requiring extensive management throughout the United States. As populations continue to grow and higher standards are placed on protecting the environment without sacrificing the supply and quality of water, water districts, public agencies, agricultural users and municipalities are faced with the challenge of managing their water supplies more efficiently.

Protecting communities from natural disasters such as floods and mudflows, cleaning natural waterways, eliminating pollution from storm runoff flowing into the ocean and protecting and enhancing natural riparian resources are among the missions of public water-managing agencies. Private developers also address these issues as part of their land development.

Transportation. Highly experienced transportation planners, engineers, and designers provide the entire spectrum of resources necessary to effectively engineer and design state-of-the-art transportation infrastructure. Engineers develop street, major arterial and highway designs in cooperation with federal, state and local agencies to improve transportation networks. Highway and interchange projects require engineering designs for roadways and interchanges for the placement or relocation of sewer and water pipelines and utility lines and for rainfall run-off management. They also require surveying services for establishment of proper rights of way for these facilities.

Energy/ Industrial

The energy/industrial industry consists of manufacturing facilities, processing facilities, power generation and distribution, and production/refining methods and systems. Power plants, machines, assembly lines, factories and refineries require mechanical, electrical and process engineering services to enable utilization of new processes and to improve efficiency and reliability of their production effort. Comprehensive engineering services that are required include:

- Design or redesign of electrical, heating, ventilation and air conditioning systems;
- Mechanical equipment design;
- Equipment selection and purchasing;
- Design of integrated computer and monitoring device systems to control manufacturing and process equipment;
- Chemical/process engineering;
- Energy generation and usage consulting;
- Fire protection engineering;
- Material handling and process flow planning;
- Automation and robotics design;
- Construction management and installation supervision;
- Plant testing during construction and start-up;
- Plant operations and maintenance;
- Project management; and
- Computer programming.

Projects that utilize mechanical, electrical and process engineering and consulting services include:

- Energy/ Power Generation and Management: power plants, natural gas/electrical systems and distribution systems;
- High Tech Facilities: biotechnology, pharmaceutical and laboratory facilities, computer centers, control rooms and research and development facilities;
- Heavy Manufacturing: automotive assembly, and pulp and paper processing;
- Consumer Products: beverage, household products, packaging, and food processing;
- Educational Facilities: school and university buildings and campuses; and
- Public Facilities/ Utilities: medical buildings, hospitals, and publicly owned or occupied buildings.

We believe there is a long-term trend in the manufacturing and assembly industries toward automation and increased efficiency. As these industries grow in the future, so does their need for engineering, design and consulting services to automate and increase the efficiency of new and existing facilities.

The Keith Companies Advantage

The engineering and consulting services industries are highly fragmented, ranging from a large number of relatively small local firms to large, multi-national firms. Management believes we are among the leading engineering and consulting services firms serving our primary industries. We believe that we can further enhance our position in the industries which we serve for the following reasons:

Reputation

We have a reputation for providing high quality services, which is strengthened due to the personal relationships developed between our staff and representatives of clients and agencies. We have been awarded many projects either due to our expertise in working with an agency or project type or because a particular client desires to work with, and can count on, specific project managers. In addition, we have received numerous awards for technical excellence including:

- Three Engineer of Merit Awards from The American Society of Civil Engineering Orange County Branch
- Water Quality Awards for Innovational Excellence from The Michigan Association of County Drain Commissioners
- Award of Excellence Honor Award from the City of Rancho Cucamonga, California for design excellence
- Engineering Project Achievement Award from the Orange County Engineering Council
- Project Achievement Award from the American Society of Civil Engineers Orange County Branch
- Outstanding Environmental Analysis Document Large Jurisdiction Award from the Association of Environmental Professionals Inland Empire Chapter
- Outstanding Environmental Analysis Document Award from the Association of Environmental Professionals
- Letter of Appreciation from the State of California Department of General Services
- Project of the Year from the Orange County Branch of the American Society of Civil Engineers

Industry and Professional Experience

We believe that our senior management has the proven ability to execute our business plan and capitalize on new opportunities. Since December 1, 1997, management has closed eight acquisitions, enabling us to diversify both our revenue base and our geographic scope. Acquisitions continue to be a key component of our business plan. In most of the acquisitions, we have retained the management teams of the acquired companies and provided the financial and management controls to promote sustainable growth. This enables the acquired management team to run their business as they know best. In addition, the entire management team, from project manager to senior executive manager, is particularly adept at the relationship side of the business that plays a critical role in the world of engineering and consulting services.

We recognize that our employees are our most valuable resource for providing continuing quality service and for obtaining new work. During employee selection and as part of the acquisition criteria, we require that the personnel whom we add to our team have significant experience in the industries that we serve. We supplement this industry experience by supporting continuing education seminars, design forums and training programs.

Full Service Approach

We provide a full complement of engineering and consulting services. Since many consulting and engineering services firms specialize in only one or a few services, a project owner may often be required to engage several engineering and/or consulting firms during the various phases of a project. The phases range from identifying and evaluating whether to acquire land or facilities, to designing, engineering and managing the construction of the finished project. In many cases, in addition to providing services during various phases of a project, we provide monitoring and maintenance services on projects after construction is complete. We believe that clients realize significant cost and time savings and maintain consistent quality by concentrating their engineering and consulting services in as few firms as practicable.

Cross-Marketing

Due to our reputation within industries we serve and due to our varied technical expertise, we have frequently increased the scope of services provided to a client from an initial engagement, such as large-scale land planning, to include other services, for example mapping, surveying and end-user site design. When we

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expand into new geographic regions, we have successfully cross-sold between our divisions and/or our various industries and intend to continue to cross-sell the services we offer.

Because our professionals provide many preliminary services for projects, we are frequently asked to provide additional services as a project progresses. In performing the preliminary services during the initial phases of a project, we obtain background information and data relating to the project that may be inefficient and costly for another firm to compile. Consequently, we are often more knowledgeable about a project, and are able to provide additional services more efficiently. As a result, we are often engaged to perform additional engineering and consulting services as a project progresses.

Effective Organizational Structure

We believe that our organizational structure allows us to compete effectively with small- and mid-sized local firms as well as with large regional, national and international firms. Our organizational structure combines the efficiencies associated with centralization and the flexibility of decentralization. When appropriate, our primary administrative functions are centralized in our corporate headquarters in Irvine, California allowing us to reduce duplicative functions and personnel at our divisional offices. We believe that this centralization allows the management at our divisional offices the freedom to focus on identifying new business opportunities and overseeing the services they provide, and also allows our project managers the flexibility to focus on being responsive to client needs. Since our divisions are managed by technical professionals with excellent client relationships and industry reputations, we promote decentralization of those aspects of our business which involve technical and client relationships.

Business Strategy

Our objective is to strengthen our position as a leading provider of engineering and consulting services while growing our geographic presence and enhancing the services we offer. To achieve this objective, we have developed a strategy with the following key elements:

Maintain High Quality Service. To maintain high quality service, we focus on being responsive to customers and working diligently and responsibly to maintain schedules and budgets. As a result of our focus on quality and timely service, we believe that we have established an excellent reputation in most of the markets we serve. We intend to continue providing high quality services as we expand our geographic presence and our service offerings.

Continue to Recruit and Retain Highly Qualified Personnel. We believe that recruiting and retaining skilled professionals is crucial to our success and growth. As a result, we intend to continue to recruit experienced and talented individuals who can provide quality services and innovative solutions.

Enhance and Strengthen Existing Client Relationships. By maintaining strong relationships with existing clients and promoting the cross-selling of services, we believe that we can further enhance our reputation and business opportunities. By focusing our efforts in this area, we can utilize the time that we spend with our clients on active work to promote additional services to them and gain additional contract opportunities for us. We believe that our existing relationships between our clients and employees is one of our greatest business development assets.

Expand Services in Public Works/ Infrastructure, and Energy/ Industrial Industries. To diminish our susceptibility to the economic cycles affecting any particular industry, we intend to continue expanding our work in public works/infrastructure and energy/industrial. Much of our expertise, including Computer Aided Drafting (CAD) work, certain engineering specialties and administrative functions, can provide support across industries in the event that a particular industry segment experiences economic downturns. We believe that by expanding our services into industries which follow different economic cycles, we are able to reassign talented employees to other project types and help provide stability for our core staff, management and profit levels. Our acquisitions of John M. Tettemer & Associates Ltd.; ESI, Engineering Services Incorporated; Thompson-Hysell, Inc.; Pacific Engineering

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Corporation; Universal Energy, Inc.; and ALNM Group Inc. have enhanced our ability to expand our services, some of which follow different economic cycles.

Expand Geographically. To diminish the impact of regional economic cycles and to further enhance cross-selling opportunities, we intend to continue to expand our geographic presence through acquisitions, possibly opening additional divisional offices and by marketing our services to clients with national and international needs. Our geographic growth may provide us with broader access to employee pools, work-sharing between regions and new business opportunities. We believe that our acquisitions of ESI, Engineering Services Incorporated; Thompson-Hysell; Crosby, Mead, Benton & Associates; Hook & Associates Engineering, Inc.; Pacific Engineering Corporation; Universal Energy, Inc. and ALNM Group, Inc. have enabled us to more effectively sell additional services in the entire Southwest and the Midwest.

Expand and Enhance Technical Capabilities. We intend to build upon our reputation as a quality provider of engineering and consulting services as we diversify our services to meet demands of our clients, industry segments and new markets. As part of our effort to continue diversifying the scope of our services, we intend to pursue strategic partnering relationships and acquisitions.

Acquisition Strategy

We intend to continue to pursue acquisitions that complement our business strategy and enhance our range of services, geographic presence and/or client base. We believe that strategic acquisitions will enable us to more efficiently serve the diverse technical and geographic needs of, and secure additional business from, national and international clients.

In general, the key criteria we consider when evaluating potential acquisitions include services offered, reputation, corporate culture, price, profitability and geographic location.

The following table sets forth information regarding our eight acquisitions since December 1, 1997:

Acquisition Date	Company Acquired	Primary Markets Currently Served	Services Offered
December 1997	ESI, Engineering Services Incorporated	Northern California	Energy/industrial services
August 1998	John M. Tettemer and Associates, Ltd.	Southern California	Water resources engineering services
July 1999	Thompson-Hysell, Inc.	Northern and Central California; Utah	Land development design & water resources engineering services
October 2000	Crosby, Mead, Benton & Associates	Southern California	Land development design, infrastructure design and landscape architecture
January 2001	Hook & Associates Engineering, Inc.	Arizona	Land development and transportation services
September 2001	Pacific Engineering Corporation	Oregon; Washington	Energy/industrial services
November 2001	Universal Energy, Inc.	National, International	Power plant operations, training, testing, and start-up
March 2002	ALNM Group, Inc.	Michigan	Environmental, water resources, and other engineering services

Consideration for the companies we have acquired has included cash, shares of our common stock, promissory notes, or a combination of these forms of consideration. The consideration is sometimes subject to earn-out or adjustment provisions. Additionally, in connection with these acquisitions, we have entered into non-competition agreements with principals of the acquired company.

Services Provided

We provide a broad range of services, including civil engineering, surveying and mapping, land planning, environmental services, cultural resources services, construction management, site acquisition, water resource engineering, and other services needed by the industrial, process and manufacturing industry, including instrumentation and control systems engineering, fire protection engineering, electrical engineering, mechanical engineering, chemical process engineering, start-up and testing, and operations and maintenance.

Civil Engineering Services

General civil engineering is often referred to as everything designed from the ground down because most of the constructed improvements involved lie on the surface of, or below the ground. Our civil engineering services include project feasibility and due diligence analysis; development cost projections; access and circulation analysis; infrastructure design and analysis; pro forma cost studies; project management; preparation of construction documents; tentative mapping; flood plain studies; sewer, water and drainage design; street and highway design; site and sub-division design; and grading design.

Surveying and Mapping Services

Surveying and mapping services include, among other things, the establishment of boundaries for preliminary engineering, construction layout, as-built surveys and the identification of features of a parcel of land that directly affect a project s design. It is common for our surveying and mapping teams to be the first in and the last out for a construction project. We provide surveying and mapping services through teams of skilled professionals that utilize sophisticated technology, including global positioning systems that utilize satellite technology to survey and navigate land, geographic information systems, and field-to-office digital and electronic data capture to produce information that serves as the foundation for a variety of planning and engineering analysis and design endeavors. We believe that we were among the first engineering and surveying consultants to utilize global positioning systems with geographic information systems to perform precise ground surveys.

Land Planning Services

Planning services include both physical planning and policy planning. Physical planning is graphical and includes conceptual drawings, sketches and layouts of communities and identifies land uses and residential and commercial neighborhoods. The resulting plan often becomes the basis for the preparation of engineering plans. To complement a physical plan, policy planning entails the preparation of supporting text and documents that establish procedures, requirements and guidelines for visual appearance or detailed permitting approvals under which the physical plan may be implemented.

Our planning services are designed to assist clients with maximizing the potential uses of real estate and other limited resources. We provide plans that take into account government regulations, effective and creative use of land assets, and the expectations and needs of the community.

Environmental Services

Our environmental services include biological studies, permit processing, environmental document preparation and mitigation monitoring. We assist clients with the complex federal, state, and local permitting process enabling them to successfully implement private and public projects. Our environmental staff offers the technical proficiency to provide one-stop preparation of environmental documents that conform to current regulatory requirements.

Our staff is experienced with the preparation of complex and challenging environmental planning documents such as Environmental Impact Reports, Environmental Impact Statements, initial studies and

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environmental assessments. Our experience includes the preparation of documents that comply with the California Environmental Quality Act (CEQA) and the National Environmental Policy Act (NEPA). Our environmental staff has been instrumental in developing permit strategy consensus among federal agencies such as the Army Corps of Engineers, U.S. Fish and Wildlife, the Environmental Protection Agency and the State of California.

Cultural Resources Services

We perform archaeological and paleontological studies that range from site review and records analysis to a discussion of measures to protect sensitive or valuable cultural resources. Further, we conduct field sampling and testing to establish or verify findings of a site review and previously documented information to determine both the quantity and quality of culturally valuable materials for a given site. Many environmental impact analyses result in requirements to protect significant cultural resources that may exist on a property, such as native American community settings, artifacts, and burial sites.

We have provided monitoring of construction activities on numerous projects and have also completed complex excavations in coordination with state and federal agencies and native American representatives.

Construction Management Services

Construction management services are an efficient bundling of some of the other services that we provide. During construction management assignments, we direct development and construction tasks, including the preparation of cost projections, entitlement and feasibility analysis, professional consultant selection and supervision, contractor bidding and construction supervision. We provide these services in discrete components or as a comprehensive package for private development and public works clients.

Site Acquisition Services

Site acquisition services include the selection of prospective properties that fit defined criteria, identifying and overcoming restrictions against the intended use of properties, negotiating agreements for the acquisition and implementing the acquisition and final use of properties. We provide site acquisition services to assist clients with obtaining the most appropriate real estate for their particular needs or to assist them in assessing the quality and reliability of existing equipment and facilities in the energy industry. For example, a property intended for the development of multi-family housing will have characteristics which vary greatly from that of a property intended for the siting of a heavy industrial facility.

Water Resources Engineering Services

Our water resources engineering services consist of financial planning, feasibility studies, storm water management, demand forecasting, hydraulic analysis and water flow studies to develop system master plans in addition to designing conventional systems of pipes, channels and dams.

Instrumentation/ Control Systems Integration Engineering Services

Our professionals integrate equipment selection, maintenance requirements and spare parts inventory by designing, selecting and reviewing mechanical, piping and electrical layouts, and providing operations and maintenance, training, start-up and emergency procedures during the design of contemporary processes or the automation of outdated manufacturing processes. These services are essential to creating an efficient operating facility.

Fire Protection Engineering Services

We provide fire protection engineering services in connection with both new construction and the renovation or modification of existing facilities to assist clients in defining and providing an acceptable level of fire safety in a cost-effective manner.

Electrical Engineering Services

These services include the design of electrical power systems for buildings, manufacturing plants and miscellaneous facilities; design of lighting systems; and selection of other equipment that delivers or uses electrical power. We design various types of electrical power generation systems and power distribution systems. We also provide cogeneration and backup emergency power supply designs for university campuses and multiple building commercial facilities.

Mechanical Engineering Services

These services are required to design energy systems, heating, ventilation, air conditioning (HVAC) systems, plumbing systems, water distribution systems and fire protection systems for facilities and buildings. We provide engineering design for HVAC systems and boiler, chilled water, compressed air, and other building facilities. Additionally, we provide mechanical engineering expertise for production line automation and manufacturing engineering support.

Chemical/ Process Engineering Services

Our chemical/ process engineers design systems for a variety of manufacturing and industrial facilities and processes like food and beverage, pharmaceutical, chemical and petroleum facilities.

Start-Up, Testing, Operations and Maintenance

As plants, whether they are power generation or wastewater treatment, are constructed they require a significant amount of testing during the construction process to insure that various functions are performing as designed and expected. This work includes testing the system processes, electrical equipment, instrument calibration, and numerous other tests to insure that the plant will function as intended when it becomes operational. It then needs to be started and monitored, and the permanent staff for the plant must be trained to operate and manage it. We provide various plant services including testing, start up, and training for power plants. In addition, we provide operations and maintenance services for water and wastewater plants and have the ability to provide the same for power plants.

Business Development and Marketing

Our business development and marketing activities consist of identifying target markets, developing strategies for pursuing these targets and supporting marketing activities company-wide by coordinating corporate promotional and professional activities. We use a client service value-added approach to our business development and marketing efforts by employing a variety of techniques to obtain contracts with new clients, repeat business with existing clients, and to maintain a positive reputation.

Additionally, our business development and marketing efforts assist our management and clients in assuring quality performance, client satisfaction, and new opportunities. To accomplish this, we provide our clients with referrals for project partners and financing sources, assist with legislative matters and monitor in-house performance. Finally, we identify new projects and prospective clients in each of the markets in which we are active. This is achieved through the use of many resources including: geographic information systems and aerial maps, project and contact databases, the Internet, lead tracking publications, and industry networking relationships. We pursue the companies, agencies, projects and markets that we believe have financial strength, long-term growth potential and established reputations.

Our growing list of services provides us with the opportunity to cross-market and sell additional services to our clients. We intend to further promote our broad service capabilities and continue to take advantage of our ability to increase our revenue by cross-selling services to existing clients and thereby to increase the number of services being provided to existing clients.

One of the keys to being successful in cross-marketing our services is to ensure that all of our managers understand the complete capabilities of our company, including our full range of services and the geographic locations and industries in which we offer and provide our services. We give presentations to our staff to educate them on our full capabilities and to encourage them to identify cross-marketing opportunities. In addition, we have implemented a formal cross-marketing program. We have produced various tools to highlight pertinent information on each of the company s divisions. These are available to all managers in each division as part of an approach geared to facilitate easy lead sharing between divisions and to maximize the effectiveness of our cross-marketing efforts. We promote successful cross-selling efforts and have been awarded numerous new or extended contracts as a direct result of this effort. In order to assist our cross-selling efforts, our divisional offices provide summaries of significant proposals to our corporate business development department for review of potential cross-selling and business enhancement opportunities.

One of our most effective methods of developing client relationships and winning new contracts has been our Executive Land Search Program. In our map rooms , we have computerized geographic information systems maps, aerial maps and city and county maps. We use these maps along with corresponding database information to identify and track a multitude of existing and potential projects. We meet with existing and prospective clients and refer available projects to them.

Clients

Our primary private sector clients consist of real estate developers, builders, major manufacturers and energy providers. Our public sector clients include water and school districts, metropolitan planning organizations, transportation authorities and local, state and federal agencies. The following is a partial list of some of our representative clients:

Real Estate	Public Works/Infrastructure
Centex Homes	Ann Arbor Transportation Authority
D.R. Horton	Central Valley Water Reclamation Facility Board
Lennar Homes	City of Anaheim, California
Pulte Home Corporation/ Del Webb	City of Fenton, Michigan
Pardee Homes	Coachella Valley Water District
Shea Homes	Inland Empire Utilities Agency
The Irvine Company	Metropolitan Water District of Southern California
Thomas & Mack Development Company	Pittsfield Charter Township, Michigan

Energy/Industrial
Bonneville Power Administration
ChevronTexaco
New United Motors Manufacturing, Inc.
University of Michigan
Weyerhaeuser Company

No individual client accounted for more than 10% of our net revenue in 2001, 2002 or 2003.

Backlog

Our gross revenue backlog for fixed price contracts and time and material contacts with not-to-exceed provisions as of December 31, 2003, was approximately $58 million as compared to $51 million at December 31, 2002. Our backlog represents an estimate of the remaining future gross revenue from existing signed contracts, and contracts which have been awarded with a defined scope of work and contract value and on which we have begun work with verbal client approval. We do not believe that backlog is fully indicative of the amount of potential future revenue that we may achieve due to the short-term nature of the contracts under which we generally provide our services compared to the long-term nature of the projects and since our contracts are subject to cancellations and/or scope adjustments.

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Competition

The market for our services is highly competitive. We compete with a variety of firms ranging from small, local firms to national and international firms that are much larger than we are. We perform engineering and consulting services for a broad spectrum of markets including energy, residential, commercial, recreational, public works, industrial, process and manufacturing. We believe that our competitive advantages include our multiple industries and services, reputation, organizational structure and business strategy. We believe that the principal factors in the engineering and consulting services selection criteria include:

- quality of service,
- relevant experience,
- staffing capabilities,
- reputation,
- geographic presence,
- stability, and
- price.

Employees

As of January 31, 2004, we had approximately 775 employees and project workers. Believing that our success depends significantly upon attracting and retaining talented, innovative and experienced professionals, we are comprised of highly skilled personnel with significant industry experience and strong client relationships. We employ licensed civil engineers, mechanical engineers, electrical engineers, land surveyors, landscape architects, certified planners, information technology specialists, power plant personnel, geodesists and archaeologists, among others.

At December 31, 2003, none of our employees were a party to a collective bargaining agreement other than approximately 10% of our employees whom we employ as field surveyors in California. Our field survey employees in our Southern California offices are covered by a Master Labor Agreement between the International Union of Operating Engineers Local Union No. 12 and the Southern California Association of Civil Engineers and Land Surveyors, which expires in October 2004. Our field survey employees in our Northern California offices are covered by a Master Agreement between the Bay Counties Civil and Land Surveyors Association and Operating Engineers Local Union No. 3, which expires in March 2005.

Available Information

We maintain a website with the address *www.keithco.com*. We are not including the information contained on our website as a part of, or incorporating it by reference into, this Annual Report on Form 10-K. We make available free of charge, through our website via a hyperlink to a third party service, our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we electronically file that material with, or furnish such material to, the Securities and Exchange Commission.

Item 2. ***Properties***

We occupy offices and facilities in various locations in California, Nevada, Utah, Arizona, Oregon, Texas and Michigan. Our corporate headquarters are located in Irvine, California and consist of approximately 63,000 square feet of space. Our corporate headquarters lease expires in October 2009. We believe that our existing office space is adequate to meet our current and foreseeable future requirements.

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Item 3. ***Legal Proceedings***

We are party to various legal proceedings that arise in the ordinary course of our business. Based on our experience, the nature of our current proceedings and our insurance policy coverage for such matters, the ultimate disposition of these matters should not have a material adverse effect on our financial position, liquidity or results of operations.

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

No matters were submitted to a vote of security holders during the quarter ended December 31, 2003.

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PART II

Item 5. ***Market for Our Common Equity and Related Stockholder Matters***

Our common stock is traded on the Nasdaq National Market under the symbol TKCI . The following table sets forth the low and high closing bid prices per share of our common stock for each calendar quarter indicated as reported on the Nasdaq National Market.

	Low	High
Year Ended December 31, 2002:		
First Quarter	$10.05	$12.91
Second Quarter	12.53	16.00
Third Quarter	9.15	15.20
Fourth Quarter	9.34	13.07
Year Ended December 31, 2003:		
First Quarter	$ 9.12	$12.83
Second Quarter	9.55	10.95
Third Quarter	9.95	13.38
Fourth Quarter	11.97	14.30

We have not declared or paid any cash dividends on our capital stock and do not anticipate paying cash dividends on our common stock in the foreseeable future. In addition, our credit agreement with our bank restricts the payment of dividends without the bank s consent.

Recent Issuances of Unregistered Securities

In connection with our acquisition of Crosby, Mead, Benton & Associates (CMB) in October 2000, the purchase agreement provided for the issuance of unregistered shares of our common stock to the former shareholders of that company, subject to certain adjustments as stated in the agreement. We issued the former shareholders of CMB 35,905 shares of our common stock with a value of $188,000 during 2001, and 32,924 shares of our common stock with a value of $253,000 during 2002. These shares were issued in transactions exempt from the registration requirements of the Securities Act of 1933, as amended, pursuant to Section 4(2) thereof.

In connection with the acquisition of Hook Associates Engineering, Inc. (Hook) in January 2001, the purchase agreement provided for the issuance of unregistered shares of our common stock to the former shareholders of that company, subject to certain adjustments as stated in the agreement. We issued the former shareholders of Hook 34,188 shares of our common stock with a value of $500,000 in 2001. These shares were issued in transactions exempt from the registration requirements of the Securities Act of 1933, as amended, pursuant to Section 4(2) thereof.

In connection with our acquisition of Universal Energy, Inc. (UEI) in November 2001, the former shareholders are eligible for additional consideration, which may affect the purchase price as a result of an earn-out provision. As part of this earn-out, which is based on certain profitability targets for 2002, 2003, and 2004, we may be obligated to issue additional shares of our common stock to be determined under the earn-out provision of the agreement. If issued, these shares are to be issued in three installments in May 2003, May 2004 and May 2005. In May 2003, we issued 70,907 shares of our common stock with a value of $714,000 related to the 2002 portion of the earn-out. UEI did not meet its profitability target related to 2003, and therefore, we do not expect to issue any shares in 2004 related to this. The issuance of future shares is subject to certain adjustments as stated in the agreement. These shares are expected to be issued in transactions exempt from the registration requirements of the Securities Act of 1933, as amended, pursuant to Section 4(2) thereof.

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In connection with our acquisition of ALNM Group, Inc. (ALNM) in March 2002, the purchase agreement provided for the issuance of unregistered shares of our common stock to the former shareholders of that company. We issued the former shareholders of ALNM 141,856 shares of our common stock in 2002 with a value of $1,569,000 and estimate approximately 75,000 shares of our common stock or $792,000 in value of shares to be issued in 2004. The issuance of future shares is subject to certain adjustments as stated in the agreement. These shares were, and are expected to be, issued in transactions exempt from the registration requirements of the Securities Act of 1933, as amended, pursuant to Section 4(2) thereof.

Item 6. ***Selected Financial Data***

The selected financial data includes the consolidated financial statement data for the periods presented.

The statement of income data for the years ended December 31, 2001, 2002 and 2003, and the balance sheet data as of December 31, 2002 and 2003, have been derived from our audited consolidated financial statements which are included elsewhere in this Annual Report on Form 10-K. The statements of income data for the years ended December 31, 1999 and 2000, and the balance sheet data as of December 31, 1999, 2000 and 2001, have been derived from our audited consolidated financial statements which are not included in this Annual Report on Form 10-K.

The following information should be read in conjunction with our consolidated financial statements and the related notes and our Management s Discussion and Analysis of Financial Condition and Results of Operations which are included elsewhere in this Annual Report on Form 10-K.

	Years Ended December 31,				
	1999	2000	2001	2002	2003
	(Dollars in thousands, except for share data)				
Statement of Income Data:					
Gross revenue	$43,084	$57,835	$74,314	$106,487	$99,950
Net revenue	39,636	53,381	66,844	91,598	90,744
Costs of revenue	26,987	34,362	42,970	59,716	58,837
Gross profit	12,649	19,019	23,874	31,882	31,907
Selling, general and administrative expenses	8,343	10,834	14,015	19,105	20,592
Income from operations	4,306	8,185	9,859	12,777	11,315
Interest income	13	31	552	384	279
Interest expense (income), net	807	341	263	(47)	15
Other expenses (income), net	29	(44)	54	(625)	(259)
Income before provision for income taxes and discontinued operations	3,483	7,919	10,094	13,833	11,838
Provision for income taxes	1,466	3,199	3,916	5,397	4,617
Income from continuing operations	2,017	4,720	6,178	8,436	7,221
Loss from discontinued operations, net of income taxes			329	628	
Net income	2,017	4,720	5,849	7,808	7,221
Reversal of redeemable securities to redemption value, net	230				

Net income available to common shareholders	$ 2,247	$ 4,720	$ 5,849	$ 7,808	$ 7,221

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	Years Ended December 31,				
	1999	**2000**	**2001**	**2002**	**2003**
	(Dollars in thousands, except for share data)				
Earnings per share from continuing operations-diluted	$ 0.50	$ 0.89	$ 0.87	$ 1.07	$ 0.91
Earnings per share diluted	$ 0.50	$ 0.89	$ 0.82	$ 0.99	$ 0.91
Weighted average shares outstanding diluted	4,515,033	5,299,679	7,092,505	7,868,877	7,957,344

	As of December 31,				
	1999	**2000**	**2001**	**2002**	**2003**
Balance Sheet Data:					
Working capital	$ 7,213	$ 7,343	$38,781	$39,613	$47,416
Total assets	23,661	33,312	71,492	82,226	87,536
Total debt, excluding issuable common stock	4,835	5,745	1,912	70	
Total shareholders equity	12,836	18,239	53,733	63,612	71,962

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Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

You should read the following discussion and analysis together with our consolidated financial statements and related notes included elsewhere in this Report. Some of the information contained in this discussion and analysis or set forth elsewhere in this Report, including information with respect to our plans and strategies for our business, includes forward-looking statements that involve risks and uncertainties. You should review the Risk Factors section of this Report for a discussion of important factors that could cause actual results to differ materially from the results described in or implied by the forward-looking statements contained in this Report.

Overview

Revenue

We derive most of our revenue from professional service activities. The majority of these activities are billed under various types of contracts with our clients, including fixed price and time-and-materials contracts. Most of our time-and-material contracts have not-to-exceed provisions. For contracts with either a fixed price or a not-to-exceed provision, revenue is recognized under the percentage of completion method of accounting based on the proportion of actual direct contract costs incurred to total estimated direct contract costs. We believe that costs incurred are the best available measure of progress towards completion on these contracts. In the course of providing services, we sometimes subcontract for various services. These costs are included in billings to clients and are included in our gross revenue. Because subcontractor services can change significantly from project to project, changes in gross revenue may not be indicative of business trends. Accordingly, we also report net revenue, which is gross revenue less reimbursable subcontractor costs. Our revenue is generated from a large number of relatively small contracts.

Costs of Revenue

Costs of revenue include labor, non-reimbursable costs, materials and various direct and indirect overhead costs including rent, utilities and depreciation. Direct labor employees work predominantly at our offices and at the clients job sites. The number of direct labor employees assigned to a contract will vary according to the size, complexity, duration and demands of the project. Contract terminations, completions, scheduling delays and contract proposal activity may result in periods when direct labor employees are not fully utilized. As we continue to grow, we anticipate that we will continue to add professional and administrative staff to support our growth. These professionals are in great demand and are likely to remain a limited resource for the foreseeable future. The significant competition for employees with the skills we require creates wage pressures on professional compensation. We attempt to increase our billing rates to customers to compensate for wage increases; however, there can be a lag before wage increases can be incorporated into our existing contracts. Some expenses, primarily long-term leases, are fixed and cannot be adjusted in reaction to an economic downturn.

Selling, General and Administrative Expenses

Selling, general and administrative expenses primarily consist of corporate costs related to finance and accounting, information technology, business development and marketing, contract proposals, executive salaries, provisions for doubtful accounts and other indirect overhead costs.

Critical Accounting Policies and Significant Estimates

The accounting policies that are most important to the portrayal of our financial condition and results of operations, and require management s most difficult, subjective or complex judgements, are considered to be our critical accounting policies. Because of the uncertainties inherent in making assumptions and estimates regarding unknown future outcomes, future events may result in significant differences between estimates and actual results. We believe that each of the assumptions and estimates are appropriate in the circumstances, and represent the most likely future outcome. The following is what we believe are the critical accounting policies most affected by management estimates and judgements.

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Revenue and Cost Recognition Estimates on Contracts. We use estimates in recognizing revenue related to our contracts with fixed price or not-to-exceed provisions. For these contracts, revenue is recognized under the percentage of completion method of accounting based on the proportion of actual direct contract costs incurred to total estimated direct contract costs. We believe that costs incurred are the best available measure of progress towards completion on these contracts. Estimating the total estimated direct contract cost is a subjective process and requires the use of our best estimates based upon the current information known by us at that point in time. Our estimate of total direct contract cost has a direct impact on the revenue recognized by us. If our current estimate of total direct contract costs turns out to be higher than our previous estimates of total direct contract cost, then we would have over recognized revenue for that previous period. Conversely, if our current estimates of total direct contract costs turns out to be lower than our previous estimates of total direct contract costs, we would have under recognized revenue for that previous period. In both cases, a job to date adjustment would be made to true-up revenue as a change in estimate applied prospectively.

Goodwill. We use estimates in order to determine if goodwill has been impaired. An impairment loss may be recognized if the carrying amount of a reporting unit s net book value exceeds the estimated fair value of the reporting unit. We arrive at the estimated fair value of a reporting unit by using a variety of customary valuation methods, such as discounted cash flow analysis and multiples of net revenue and earnings before interest and taxes. These valuation methods use a variety of assumptions such as future billable employee headcount, net revenue per billable employee, operating income, cash flow, discount rates and multiples. Estimating fair value of a reporting unit is a subjective process and requires the use of our best estimates. We will perform our valuation analysis at least annually or if an event occurs or circumstances change that would indicate the carrying amount of goodwill may be impaired. If our estimates or assumptions change from those used in our current valuation, we may be required to recognize an impairment loss in future periods.

Provision for Doubtful Accounts. We use estimates in arriving at our allowance for doubtful accounts related to our contracts and trade receivables. These estimates are based on our best assessment as to the collectibility of the related receivable balance. Each quarter, we re-evaluate our estimates to assess the adequacy of our allowance for doubtful accounts and adjust the allowance for doubtful accounts as necessary. Factors considered in arriving at our allowance for doubtful accounts, include among other things, historical and anticipated client default rates at the various aging categories of contract and trade receivables and the overall business environment/ economy. Future collections of receivables that are different from our current estimates will affect results of operations in future periods.

Discretionary Bonus Plan. During 2003, we implemented a discretionary bonus plan. Under this bonus plan, we may award an annual cash performance bonus to our employees provided that our annual actual results exceed a pre-established annual target. We review the need for a bonus accrual on a quarterly basis by comparing our actual quarterly results and our estimated results for the remainder of the year to our annual pre-established target. Estimating our future results is a subjective process and requires the use of our best estimates based upon the current information known to us at that point in time. As a result of potential changes to our estimates, our quarterly results may be significantly affected by adjustments to the bonus accrual. In the fourth quarter of 2003, we made our final adjustment to the 2003 bonus accrual. Any annual bonus award under this plan is at the discretion of the Compensation Committee of the Board of Directors.

Impact of Our Industry Diversification Strategy

To help reduce our susceptibility to economic cycles affecting the real estate development industry, we intend to expand our work in the public works/ infrastructure and the energy/ industrial industries as feasible, based upon such items as economic and market conditions. We believe that among other business initiatives, our acquisition strategy may play a significant role in contributing to this objective. The acquisitions of Pacific Engineering Corporation (PEC) and Universal Energy Inc. (UEI) during 2001, ALNM Group, Inc. (ALNM) in 2002 and anticipated future acquisitions, many of which may include engineering services outside of the real estate development industry, may have a significant impact on our future net revenue mix. Due to these and potential future acquisitions, we anticipate that our margins may be affected by the decreased business concentration from the real estate development industry which has historically yielded higher margins than services provided to the public works/ infrastructure and energy/ industrial industries.

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Results of Operations

The following table sets forth supplemental consolidated operating results for each of the periods presented as a percentage of net revenue:

	Years Ended December 31,		
	2003	2002	2001
Gross revenue	110.1%	116.3%	111.2%
Subcontractor costs	10.1	16.3	11.2
Net revenue	100.0	100.0	100.0
Costs of revenue	64.8	65.2	64.3
Gross profit	35.2	34.8	35.7
Selling, general and administrative expenses	22.7	20.9	21.0
Income from operations	12.5	13.9	14.7
Interest income	0.3	0.4	0.8
Interest expense (income), net	0.0	(0.1)	0.3
Other (income) expenses, net	(0.3)	(0.7)	0.1
Income before provision for income taxes and discontinued operations	13.1	15.1	15.1
Provision for income taxes	5.1	5.9	5.9
Income from continuing operations	8.0	9.2	9.2
Loss from discontinued operations, net of income taxes	0.0	(0.7)	(0.4)
Net income	8.0%	8.5%	8.8%

The following table sets forth the Company s consolidated statements of income for the years ended December 31, 2003 and 2002 and includes the dollar and percentage change:

	Years Ended December 31,			
	2003	2002	$ Change	% Change
	(Dollars in thousands)			
Gross revenue	$ 99,950	$ 106,487	$ (6,537)	(6.1)%
Subcontractor costs	9,206	14,889	(5,683)	(38.2)
Net revenue	90,744	91,598	(854)	(0.9)
Costs of revenue	58,837	59,716	(879)	(1.5)
Gross profit	31,907	31,882	25	0.1
Selling, general and administrative expenses	20,592	19,105	1,487	7.8
Income from operations	11,315	12,777	(1,462)	(11.4)
Interest income	279	384	(105)	(27.3)
Interest expense (income), net	15	(47)	(62)	(131.9)

Other (income) expenses, net	(259)	(625)	(366)	(58.6)
Income before provision for income taxes and discontinued operations	11,838	13,833	(1,995)	(14.4)
Provision for income taxes	4,617	5,397	(780)	(14.5)
Income from continuing operations	7,221	8,436	(1,215)	(14.4)
Loss from discontinued operations, net of income taxes		628	628	(100.0)
Net income	$ 7,221	$ 7,808	$ (587)	(7.5)%

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Years Ended December 31, 2003 and December 31, 2002

Net Revenue. Net revenue for 2003 decreased $0.9 million, or 0.9%, to $90.7 million compared to $91.6 million for 2002. This decrease in net revenue was partially offset by $1.4 million in additional net revenue during 2003 related to the acquisition of ALNM Group, Inc. (ALNM), in March 2002, as compared to the same period in 2002. Excluding the net revenue from the ALNM acquisition, net revenue decreased by $2.3 million, or 2.5%. This decrease was primarily a result of a continued slowdown in our energy/ industrial industry segment due to a slowdown in the pace of construction of new power plants and/or alternative power solutions and a general decrease in capital spending in the energy/ industrial industry, coupled with the completion of a large contract in our energy/industrial segment which had significant activity during 2002, and lower net revenue from our Arizona office, which was part of the acquisition of Hook & Associates Engineering, Inc. (Hook) in January 2001. The decline in net revenue was partially offset by increased net revenue generated from our real estate services due to a strong California residential real estate market.

Subcontractor costs, as a percentage of net revenue, decreased to 10.1% during 2003 as compared to 16.3% during 2002. The decrease was primarily due to a decrease in subcontractor costs related to several large contracts in 2002 in our energy/ industrial segment.

Market uncertainties in the power generation portion of the energy industry have caused a decline in the pace of construction of new power plants and/or alternative power solutions and a general decrease in capital spending in the energy/ industrial industry. As a result, our energy/ industrial segment continued to experience a reduction in net revenue during 2003. If this market uncertainty continues, it may cause further reductions in net revenue and therefore continue to negatively impact net income from our energy/ industrial segment.

Although we have not experienced a significant decrease in net revenue from our public works/ infrastructure industry during 2003 as compared to 2002, certain current conditions, including a weak economy in the public works/ infrastructure industry, especially in the Greater Southeast Michigan area, lead us to believe that we may experience an adverse impact to net revenue and net income related to this industry.

Gross Profit. Gross profit for 2003 remained flat at $31.9 million compared to 2002. Excluding the additional 2003 gross profit of $0.3 million generated from the acquisition of ALNM in March 2002, gross profit decreased by $0.3 million. This decrease was mainly due to lower gross profit from our energy/ industrial segment, along with the completion of a large contract in our energy/ industrial segment which had significant activity during 2002, and $0.4 million of additional expense related to the discretionary bonus plan. These decreases were offset by strong gross profit from our real estate services. For 2003, gross profit as a percentage of net revenue increased to 35.2% as compared to 34.8% during 2002. This increase was primarily due to strong gross profit from our real estate services, which was partially offset by lower gross profit from our energy/ industrial segment.

As noted above, due to a continuing decline in the pace of construction of new power plants and/or alternative power solutions and a general decrease in capital spending in the energy/ industrial industry, our energy/ industrial segment experienced a reduction in its gross profit during 2003. If this decline continues, it may cause our energy/ industrial segment to experience a continued reduction of gross profit and therefore also a reduction in net income.

We have experienced a slight decrease in gross profit from our public works/ infrastructure industry during 2003 as compared to 2002. Certain current conditions, including a weak economy in the public works/ infrastructure industry, especially in the Greater Southeast Michigan area, lead us to believe we may experience a further decline in our gross profit and net income related to this industry.

Selling, General and Administrative Expenses. During 2003, selling, general and administrative expenses (SG&A) increased $1.5 million, or 7.8%, to $20.6 million compared to $19.1 during 2002. The increase in SG&A during 2003 was primarily due to the increase in SG&A costs attributable to ALNM, and increases in: legal fees, proposal activities, employee placement fees for new hires, and the provision for doubtful accounts. During 2003, SG&A as a percentage of net revenue increased to 22.7% compared to 20.9% during 2002 primarily due to increases in the items discussed above.

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Interest Income. Interest income during 2003 decreased by $105,000 as compared to 2002. This decrease in interest income resulted from lower yields earned on cash and securities, partially offset by an increase in the average balance of cash and securities as compared to 2002.

Interest Expense. Interest expense during 2003 increased by $62,000 compared to 2002. The increase in interest expense was primarily attributable to a $130,000 reduction of interest expense during 2002 associated with an acquisition modification agreement related to Hook which resulted in the cancellation of a $1.3 million acquisition note payable.

Other (Income) Expenses, net. Other income during 2003 decreased by $366,000 as compared to 2002. This decrease was primarily associated with a $687,000 increase in other income during 2002 resulting from purchase price adjustments in connection with the acquisitions of Crosby Mead Benton & Associates (CMB) and Hook. This decrease was partially offset by a net $230,000 sublease termination fee recognized by us during 2003 related to one of our facilities which we had subleased and $73,000 in other income recognized during 2003 associated with a purchase price adjustment related to the acquisition of ALNM.

Income Taxes. The provision for income taxes during 2003 was $4.6 million compared to $5.4 million for 2002. This decrease in provision for income taxes during 2003 resulted from a lower taxable base. Our effective tax rate was 39% during 2003 and 2002.

Discontinued Operations. We closed down the operations of three divisions during 2002. Two of these divisions were part of our operations in Colorado and Wyoming from our acquisition of Hook, and the third was our internally created Communication division located in California. In accordance with accounting principles generally accepted in the United States of America, the activities of these divisions were segregated and reported as discontinued operations during 2002.

The following table sets forth the Company s consolidated statements of income for the years ended December 31, 2002 and 2001 and includes the dollar and percentage change:

	Years Ended December 31,			
	2002	2001	$ Change	% Change
	(Dollars in thousands)			
Gross revenue	$106,487	$74,314	$32,173	43.3%
Subcontractor costs	14,889	7,470	7,419	99.3
Net revenue	91,598	66,844	24,754	37.0
Costs of revenue	59,716	42,970	16,746	39.0
Gross profit	31,882	23,874	8,008	33.5
Selling, general and administrative expenses	19,105	14,015	5,090	36.3
Income from operations	12,777	9,859	2,918	29.6
Interest income	384	552	(168)	(30.4)
Interest (income) expense, net	(47)	263	310	117.9
Other (income) expenses, net	(625)	54	679	1,257.4
Income before provision for income taxes and discontinued operations	13,833	10,094	3,739	37.0
Provision for income taxes	5,397	3,916	1,481	37.8
Income from continuing operations	8,436	6,178	2,258	36.5
Loss from discontinued operations, net of income taxes	628	329	299	90.9
Net income	$ 7,808	$ 5,849	$ 1,959	33.5%

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Years Ended December 31, 2002 and December 31, 2001

Net Revenue. The growth in net revenue for 2002 compared to 2001 is primarily attributable to acquisitions, which contributed $22.5 million in net revenue. The acquired companies mainly contributing to this net revenue growth include: PEC, UEI, and ALNM, whose operations have been included in the consolidated financial statements since October 2001, December 2001 and March 2002, respectively. Excluding the net revenue from these acquisitions, net revenue increased by $2.2 million, or 3.3%, compared to 2001. The increase in net revenue, excluding acquisitions, primarily resulted from (i) a strong Southern California residential real estate market, which continued to experience an increase in demand, and (ii) higher net revenue derived from the Company s water resource services. These increases were partially offset by a decrease in net revenue generated by the Company s Arizona office which is part of the Hook operations coupled with lower net revenue generated from the Company s Orange County office resulting mainly from a continued weak commercial and industrial real estate market. Subcontractor costs, as a percentage of net revenue, increased to 16.3% during 2002 compared to 11.2% during 2001, resulting largely from an increase in subcontractor costs related to several large contracts in the energy/ industrial industry.

Difficulties in the power generation segment of the energy industry have caused a decline in the pace of construction of new power plants and/or alternative power solutions. As a result, our energy/ industrial industry began to experience a reduction in net revenue during the fourth quarter of 2002. If the difficulties continue, they may cause further reductions in net revenue and therefore net income in our energy/ industrial industry.

Gross Profit. The increase in gross profit was mainly attributable to acquisitions, which added gross profit of $7.2 million during 2002 compared to the prior year. Excluding the gross profit from acquisitions, gross profit increased $0.8 million or 3.4% during 2002 as compared to 2001. This increase was primarily attributable to strong gross profit resulting from continued demand for residential real estate in Southern California and higher gross profit generated from the Company s water resource services, all of which were partially offset by lower gross profit from (i) the Hook Arizona office, (ii) one of our Northern California offices, and (iii) our UEI division, as mentioned above.

As a percentage of net revenue, gross profit decreased to 34.8% during 2002 from 35.7% during 2001. The percentage decrease was primarily related to lower margins related to the Company s energy/ industrial industry, the Hook Arizona office, and ALNM which mainly provides services in the public works/ infrastructure industry.

The increase in the costs of revenue was primarily attributable to increased expenses associated with the growth in our total direct employee base, which grew from an average of 510 in 2001 to 673 in 2002. This increase is primarily a result of acquisitions.

As noted above, due to a continuing decline in the pace of construction of new power plants, and/or alternative power solutions, our energy/ industrial industry experienced a reduction in its gross profit in the fourth quarter of 2002. If this decline continues, it may cause our energy/ industrial industry to experience a continued reduction of gross profits and therefore also a reduction in net income.

Selling, General and Administrative Expenses. The increase in selling, general and administrative expenses was primarily related to acquisitions, an increase in corporate administrative costs, and an increase in the provision for doubtful accounts, all of which were partially offset by the elimination of goodwill amortization, as compared to 2001. Acquired companies contributed $3.9 million of additional selling, general and administrative expenses in 2002 as compared to 2001. As a percentage of net revenue, selling, general and administrative expenses decreased slightly to 20.9% during 2002 from 21.0% during 2001, mainly from the elimination of goodwill amortization which was partially offset by the increase in the provision for doubtful accounts.

Interest Income. The decrease in interest income resulted from lower yields on cash and securities, partially offset by an increase in the average balance of cash and securities as compared to 2001.

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Interest Expense. The decrease in interest expense was primarily attributable to a reduction of interest expense associated with the acquisition modification agreement (as discussed under the Liquidity and Capital Resources section) related to Hook, which resulted in the cancellation of a $1.3 million acquisition note payable and the overall reduction of debt as compared to 2001.

Other Income (Expenses), net. The increase in other income was primarily associated with $687,000 resulting from a purchase price adjustment in connection with the acquisitions of CMB and Hook.

Income Taxes. The increase in provision for income taxes resulted primarily from higher pre-tax income and a slightly higher effective tax rate during 2002. Our effective income tax rate was approximately 39.0% during 2002 compared to 38.8% during 2001.

Discontinued Operations. The loss from discontinued operations is attributable to the closure of three of our divisions during 2002. Two of these divisions related to our Hook operations located in Colorado and Wyoming, and, the third was our internally created Communication division which was located in California. In accordance with accounting principles generally accepted in the United States of America, the activities of these divisions have been segregated and reported as discontinued operations during 2002 and 2001. The increase in the loss from discontinued operations was mainly due to continuing difficult market conditions and deteriorating operating results in Colorado.

Related Party

In March 2001, we entered into change in control agreements with Aram H. Keith, our chief executive officer and chairman of the board, Eric C. Nielsen, our president and chief operating officer, and Gary C. Campanaro, our chief financial officer and secretary, and a director of our company. These agreements provide that if the executive officer s employment with us terminates as a result of an involuntary or constructive termination (as these terms are defined in the agreements) at any time within two years following a change in control, then, in addition to other benefits, the executive officer will receive a one-time payment, equal to two times the executive officer s highest annual level of total cash compensation (including any and all bonus amounts) paid by us to that executive officer during any one of the three consecutive calendar years (inclusive of the year of termination) immediately prior to termination. The executive officer also is entitled to receive a payment by us to offset any excise tax under the Internal Revenue Code of 1986, as amended, that has been levied against the executive officer for payments that we have made to him. In addition, any unvested options previously granted to the executive officer will immediately vest and become exercisable as of the date of termination and remain exercisable until their respective expiration dates.

We have not entered into any material related party transactions during 2003.

Liquidity and Capital Resources

Cash and cash equivalents combined with securities held-to-maturity totaled $28.9 million as of December 31, 2003, compared to $23.5 million as of December 31, 2002, an increase of $5.4 million. Working capital as of December 31, 2003 was $47.4 million compared to $39.6 million as of December 31, 2002, an increase of $7.8 million. Our debt to equity ratio (excluding the effect of issuable common stock) at both December 31, 2003 and December 31, 2002 was 0.00 to 1.

Cash Flows From Operating Activities. Net cash provided by operating activities decreased $2.7 million, to $7.4 million during 2003 compared to $10.1 million during 2002. The decrease in net cash provided by operating activities during 2003 as compared to 2002 was primarily the result of lower net income, partially offset by a purchase price adjustment and changes in operating assets and liabilities, net of effects from acquisitions.

Cash Flows From Investing Activities. Net cash used in investing activities totaled $3.6 million for 2003 compared to $1.4 million for 2002, an increase of $2.2 million. This increase in net cash used in investing activities was primarily due to a significant increase in cash used to purchase securities held-to-maturity, substantially offset by a decrease in cash used for acquisitions.

Cash Flows From Financing Activities. Net cash provided by financing activities increased by $789,000 to $243,000 for 2003 compared to net cash used in financing activities of $546,000 for 2002. This increase in net cash provided by financing activities resulted primarily from a decrease of principal payments on our debt and capital lease obligations during 2003.

The Company has available a $10.0 million unsecured line of credit consisting of four components: (i) an acquisition component, (ii) an equipment and vehicle financing component, (iii) a standby letter of credit component, and (iv) a working capital component. The line provides up to a maximum of $5.0 million to finance acquisitions, up to a maximum of $3.0 million to finance equipment and vehicle purchases, up to a maximum of $1.0 million for standby letters of credit, and up to a maximum of $10.0 million less the aggregate outstanding principal balance of the acquisition, equipment and vehicle, and standby letter of credit components for working capital. The line bears interest at either a range of 0.25% below prime to prime, or a range of 1.25% to 1.75% over LIBOR depending on the Company s ability to meet certain financial covenants. All components of the line of credit mature in June 2005. This line of credit agreement restricts the payment of dividends without the bank s consent. As of December 31, 2003, the Company had utilized the letter of credit component of this line of credit to issue a $229,000 stand-by letter of credit. The Company did not have any outstanding balances under this line of credit agreement as of December 31, 2002.

Our financial statements for 2003 reflect the reduction of the purchase price of ALNM which we acquired in March 2002. Under the terms of the purchase agreement, the obligation to issue $1.5 million in shares of our common stock was reduced to approximately $0.8 million.

On occasion, we will enter into purchase agreements related to acquisitions which provide for future purchase price payments or earn-outs as a result of achieving certain operating results by the acquired companies. As a result of these earn-out provisions, we may be obligated to pay additional consideration in future periods. Current accounting principles require that these earn-outs be accrued on our balance sheet only at the point at which the earn-out period has elapsed and the performance targets have been met. As of December 31, 2003, we have one year remaining on an earn-out and we may be obligated to pay a maximum of $7.4 million in additional purchase price related to our acquisitions, of which 50% will be paid in cash with the remaining 50% to be paid out in our common stock. Such potential earn-outs are not currently reflected on our balance sheet as the earn-out period has not elapsed and, therefore, the achievement of the performance target is currently unknown.

We do not hold any derivative financial instruments for trading purposes or otherwise. In addition, we presently do not enter into any hedging type activities to manage our exposure to foreign currency risk associated with our Brazilian operation. Our Brazilian operation, which provides services to our energy/ industrial segment, generated approximately $0.5 million in net revenue during 2003. Furthermore, we have not engaged in energy or commodity trading activities and do not anticipate doing so in the future, nor do we have any transactions involving unconsolidated entities, special purpose entities, or variable interest entities.

The following summarizes our contractual obligations as of December 31, 2003, and the effect such obligations are expected to have on liquidity and cash flows in the future.

	Payments Due by Period				
	Total	**Less Than 1 Year**	**1 - 3 Years**	**3 - 5 Years**	**More Than 5 Years**
Operating lease obligations	$13,724,000	$3,808,000	$6,072,000	$2,866,000	$978,000
Total contractual cash obligations	$13,724,000	$3,808,000	$6,072,000	$2,866,000	$978,000

Future Cash Requirements

We expect to fund our future liquidity needs primarily from (i) operating cash flows, (ii) existing balances of cash and cash equivalents and securities held-to-maturity, and (iii) borrowings under our $10.0 million unsecured revolving line of credit, which we have not utilized as of December 31, 2003 other than to issue a $229,000 stand-by letter of credit. We believe these sources of funds will be sufficient to provide

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for our operations and planned capital expenditures and satisfy our debt obligations over the next twelve months. We expect our capital expenditures in fiscal 2004 to range between approximately $2.0 million to $3.0 million.

We also intend to use available liquidity to continue our acquisition strategy. We continue to examine acquisitions of complementary businesses and anticipate that our liquidity will be sufficient to provide for potential acquisitions for the next twelve months. However, the pace and size of acquisitions are difficult to predict. We may complete more or fewer acquisitions than we currently contemplate depending on the opportunities that present themselves, and our cash requirements may change accordingly.

Effect of Recent Accounting Pronouncements

In May 2003, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards (SFAS) No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity.* SFAS No. 150 requires issuers to classify as liabilities (or assets in some circumstances) three classes of freestanding financial instruments that embody obligations for the issuer. The provisions of this statement are effective for financial instruments entered into or modified after May 31, 2003 and are otherwise effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of this statement did not have a material effect on our financial condition, results of operations, or cash flows.

In April 2002 and July 2002, the Financial Accounting Standard Board (FASB) issued Statements of Financial Accounting Standard No. 145, Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections (SFAS 145), and No. 146 Accounting for Costs Associated with Exit or Disposal Activities (SFAS 146), respectively. SFAS 145 prescribes amendments to existing pronouncements on accounting for early retirements of debt. The provisions of this statement are effective for financial statements issued on or after May 15, 2002. SFAS 146 addresses issues pertaining to costs associated with exit or disposal activities initiated after December 31, 2002. The adoption of these standards did not have a material effect on the Company s financial condition, results of operations or cash flows.

Inflation

Although our operations can be influenced by general economic trends, we do not believe that inflation had a significant impact on our results of operations for the periods presented. Due to the short-term nature of most of our contracts, if costs of revenue increase, we will attempt to pass these increases on to our clients; however, there can be a lag before these increases in costs can be incorporated into our existing contracts.

The following discussion summarizes material risks which you should carefully consider before you decide to invest in our common stock or to maintain or increase your investment. Any of the following risks, if they actually occur, would likely harm our business. The trading price of our common stock could then decline, and you may lose all or part of the money you paid to buy our common stock.

Risk Factors Risks Related To Our Industries

Our business could suffer if there is a downturn in the real estate market

During 2003, approximately 67% of our net revenue was rendered in connection with commercial and residential real estate development projects. Reduced demand in the real estate market would likely decrease the demand for our services. A decrease in the demand for our services could result in cash flow difficulties and potential operating losses for our company.

The real estate market and, therefore, our business, may be impacted by a number of factors, which may include:

changes in employment levels and other national and local economic conditions;

changes in interest rates and in the availability, cost and terms of financing;

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the impact of present or future environmental, zoning or other laws and regulations;

changes in real estate tax rates and assessments and other operating expenses;

changes in levels of government spending and fiscal policies; and

earthquakes and other natural or manmade disasters and other factors which are beyond our control.

We derive revenue from contracts with government agencies. Any disruption in government funding or in our relationship with those agencies could adversely affect our business

The demand for our services is related to the level of government program funding that is allocated to rebuild, improve and expand the nation s infrastructure. We believe that the success and further development of our business depends, in part, upon the continued funding of these government programs and upon our ability to participate in these government programs. We cannot assure you that governments will have the available resources to fund these programs, that these programs will continue to be funded even if governments have available financial resources or that we will continue to win government contracts.

Some of these government contracts are subject to renewal or extensions annually, so we cannot be assured of our continued work under these contracts in the future. Unsuccessful bidders may protest or challenge the award of these contracts. In addition, government agencies can terminate these contracts at their convenience. As a result, we may incur costs in connection with the termination of these contracts and suffer a loss of business. Also, contracts with government agencies are subject to substantial regulation and an audit of actual costs incurred. Consequently, there may be a downward adjustment to our revenue if billed recoverable costs exceed actual recoverable costs.

We derive revenue from engineering services provided to the energy industry. Continued delay and reduction in the pace of construction for new power plants, cogeneration facilities, and electrical distribution facilities has had, and may continue to have an adverse affect on our business

The demand for our services is related to the level and pace of construction of energy related solutions. We believe that the success and further development of this aspect of our business depends, in part, upon the need for and funding of these projects. High energy prices, power shortages, and pressure at state and federal levels for increased supply resulted in the increased demand for energy related solutions with an unprecedented number of new power plants, cogeneration facilities, and electrical distribution facilities announced in 2001. However, a weakening demand and softening economy combined with a decline in energy prices have caused builders of such energy related solutions to reconsider planned projects. Many have announced downsizings or cancellations of new power plants and/or alternative power solutions. The decline in the pace of construction of new power plants and/or alternative power solutions has had, and may continue to have, an adverse affect on our energy/industrial segment.

We may have difficulty in attracting and retaining qualified professionals, which may harm our reputation in the marketplace and restrict our ability to implement our business strategy

We derive our revenue almost exclusively from services performed by our professionals. We may not be able to attract and retain the desired number of professionals over the short or long-term. There is significant competition for professionals with the skills necessary for the provision of our services from major and boutique consulting, engineering, research and other professional service firms. We believe that our existing relationships between our clients and our employees is one of our greatest business development assets. Our inability to attract and retain qualified professionals could impede our ability to secure and complete engagements, in which event, we may lose market share and our revenue and profit may decline.

Terrorism and related conflicts may have a material adverse effect on our operating results

The terrorist attacks that took place in the United States on September 11, 2001, along with the United States military campaign against terrorism in Afghanistan, Iraq and elsewhere, and ongoing violence in the Middle East have created many economic and political uncertainties, some of which had and may materially affect the markets in which we operate, and our operations and profitability. The short-term and long-term effects of these developments on our customers, the markets for our services and the U.S. economy are uncertain. The consequences of any terrorist attacks, or any armed conflicts, are unpredictable, and we may not be able to foresee events that could have an adverse effect on our markets, or our business.

Risk Factors   Risks Related To Our Business

Our revenue, income and cash flow could decline if there is a downturn in the California economy or real estate market

During 2003, approximately 72% of our net revenue was derived from services rendered in California. Poor economic conditions in California may significantly reduce the demand for our services and decrease our revenue and profits. From 1991 to 1996, our business was negatively impacted during the real estate market downturn in Southern California, and we experienced cash flow difficulties and substantial operating losses.

If we are unable to effectively manage our growth, we could incur unforeseen costs or delays and our reputation and reliability in the marketplace could be damaged

We have grown rapidly and intend to pursue further growth, through acquisitions and otherwise, as part of our business strategy but we may not be able to manage our growth effectively and efficiently. Our inability to manage our growth effectively and efficiently could cause us to incur unforeseen costs, time delays or other negative impacts, any of which could cause a decline in our revenue and profitability. Our rapid growth has presented and will continue to present numerous administrative and operational challenges, including the management of an expanding array of engineering and consulting services, the assimilation of financial reporting systems, increased pressure on our senior management and increased demand on our systems and internal controls.

If we are unable to successfully implement our acquisition strategy, we may not meet our current expectations of growth and/or operating results

Our growth strategy includes the strategic acquisition of companies that expand our service offerings and geographic presence, including acquisitions that may be larger than our historic acquisitions. If we are unsuccessful in implementing our acquisition strategy, we could fail to achieve the revenue and profitability growth that we currently expect. We may not be successful in implementing our acquisition strategy for a number of reasons, including the following:

We may fail to consummate an acquisition even if an announcement had been made to acquire a target company;

As the engineering industry consolidates, suitable acquisition candidates are expected to become more difficult to locate and may only be available at an increased price or under terms that are less favorable than in the past;

We may not be able to arrange suitable financing to consummate an acquisition;

We may not be successful in integrating an acquired company s professionals, clientele and culture into ours;

We may not be successful in generating the same level of operating performance that an acquired company experienced prior to the acquisition;

As we expand our service offerings and geographic presence, we may not be able to maintain the current level of quality of services;

We may not be able to maintain our reputation in an acquired entity s geographic area or service offerings and as a consequence our ability to attract and retain clients in those or other areas may be negatively impacted;

An acquired company may be less profitable than us resulting in reduced profit margins; and

The acquisition and subsequent integration of an acquired company may require a significant amount of management s time, diverting their attention from our existing operations and clients, which could result in the loss of key employees or clients.

If our estimates or assumptions used in arriving at the fair value of acquired entities change from those used in our current valuations, we may be required to recognize a goodwill impairment loss

We use estimates in order to determine if goodwill has been impaired. An impairment loss may be required to be recognized if the carrying amount of a reporting unit s net book value exceeds the estimated fair value of the reporting unit. We arrive at the estimated fair value of a reporting unit by using a variety of customary valuation methods, such as discounted cash flow analysis and multiples of net revenue and earnings before interest and taxes. These valuation methods use a variety of assumptions such as future billable employee headcount, net revenue per billable employee, operating income, cash flow, discount rates and multiples. Estimating fair value of a reporting unit is a subjective process and requires the use of our best estimates. If our estimates or assumptions change from those used in our current valuation, we may be required to recognize an impairment loss. As of December 31, 2003, our goodwill balance, net of accumulated amortization was $23.1 million. We no longer amortize goodwill due to our adoption of SFAS No. 142 Goodwill and Other Intangible Assets.

We could lose money if we fail to accurately estimate our costs on fixed-price contracts and/or contracts with not-to-exceed provisions

We expect to perform services under contracts that may limit our profitability. Under fixed-price contracts we perform services at a stipulated price. Under time-and-materials contracts with not-to-exceed provisions, we are reimbursed for the number of labor hours expended at an established hourly rate plus the cost of materials incurred, subject, however, to a stated maximum dollar amount for the services to be provided under the contract. In both of these types of contracts, we agree to provide our services based on our estimate of the costs a particular project will involve. Our estimates are not always accurate. Underestimation of costs for these types of contracts may cause us to incur losses or result in a project not being as profitable as we expected. We may fail to estimate costs accurately for a number of reasons, including:

weakness in the management of our projects;

loss of efficiency resulting from cross-utilization of office staff from various locations;

changes in the costs of goods and services that may occur during the contract period;

problems with new technologies; and

delays beyond our control.

Our backlog is an uncertain indicator of future financial performance and is subject to adjustment or cancellation

Our gross revenue backlog for fixed price contracts and time-and-materials contracts with not-to-exceed provisions as of December 31, 2003 was approximately $57.9 million. We cannot assure you that the entire balance of our backlog will convert into revenue since our contracts are subject to scope adjustments and/or cancellations. These types of scope adjustments or cancellations may result in a reduction in our backlog which could adversely affect our revenue and profit.

The loss of Mr. Keith could adversely affect our business, including our ability to secure and complete engagements and attract and retain employees

We do not have an employment agreement with, or maintain key man life insurance on Aram H. Keith, our chief executive officer. If we lose the services of Mr. Keith, we may be less likely to secure or complete contracts and to attract and retain additional employees. The efforts, abilities, business generation capabilities and name recognition of Mr. Keith are important to our success in those activities.

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If our employees leave our company and join a competitor, we may lose business

Our employees might leave our company and become competitors of ours. If this happens, we may lose additional employees and some of our existing clients that have formed relationships with our former employees. In addition, we may lose future clients to a former employee as a new competitor. In either event, we could lose clients and revenue, and our profitability could decline.

Adverse weather conditions or acts of God may cause a delay or elimination of our net revenue otherwise recognized and adversely affect our profitability

Field activities are generally performed outdoors and may include surveying, archeology, plant start-up and testing, and plant operations. Certain weather conditions or acts of God (such as fire, floods, etc.) may cause postponements in the initiation and/or completion of our field activities and/or may hinder the ability of our office employees to arrive at work, which may result in a delay or elimination of revenue that otherwise would have been recognized, while certain costs will continue to be incurred. Adverse weather conditions or acts of God may also delay or eliminate our initiation and/or completion of the various phases of work relating to our other engineering services that commence concurrent with or subsequent to field activities. Any delay in completion of the field, office and/or other activities may require us to incur additional costs attributable to overtime work necessary to meet the client s required schedule. Due to various factors, a delay in the commencement or completion of a project may also result in a cancellation of the contract. As a result, our net revenue and profitability may be adversely affected.

Our business may expose us to liability in excess of our current insurance coverage

We are exposed to potential liabilities to clients for errors or omissions in the services we perform. These liabilities could exceed our current insurance coverage and the fees we derive from those services. We cannot always predict the magnitude of these potential liabilities but claims could be significant. A partially or completely uninsured claim, if successful and of significant magnitude, could result in substantial losses.

We currently maintain general liability, umbrella, professional liability, directors and officers liability, and various types of other insurance policies. Claims may be made against us which exceed the limits of these policies, in which case we would be liable to pay these claims from our assets. Our professional liability and directors and officers liability policies are claims made policies and only claims made during the term of the policy are covered. If we terminate our policies and do not obtain retroactive coverage, we would be uninsured for claims made after termination even if these claims are based on events or acts that occurred during the term of the policy. Our insurance policies typically have various exceptions to the claims covered and also require us to assume some costs of the claim even though a portion of the claim may be covered, resulting in potential liability to us. Further, our expansion into new services or geographic areas could result in our failure to obtain coverage for these services or areas, or the coverage being offered may be at a higher cost than our current coverage. Due to the current insurance environment, we have experienced and may continue to experience an increase in our insurance premiums. We may not be able to pass these increases on to our clients in increased billing rates.

If we are unable to engage qualified subcontractors, we may lose projects, revenue and clients

We often contract with outside companies to perform designated portions of the services we perform for our clients. If we are unable to engage subcontractors, our ability to perform under some of our contracts may be impeded and the quality of our service may decline. As a consequence, we may lose projects, revenue and clients. Subcontractor costs accounted for approximately 10% of our net revenue during 2003.

We derive revenue from contracts for work performed in foreign countries which are subject to a number of risks that could adversely affect the results from these contracts

International business is subject to the customary risks associated with international transactions, including political risks, local law and taxes, difficulty in enforcing contracts, the potential imposition of trade or currency exchange restrictions, tariff increases and difficulties or delays in collecting accounts receivables.

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Weak foreign economies and/or a weakening of foreign currencies against the U.S. dollar could have a material adverse effect on our business, financial condition and results of operations. We presently do not enter into any hedging type activities to manage our exposure to foreign currency risk associated with our Brazilian operations.

Risk Factors Risks Related To Ownership of Our Stock

Our stock price may decrease, which could result in significant losses for investors or adversely affect our business

The following factors could cause the market price of our common stock to decrease, perhaps substantially:

- the failure of our quarterly operating results to meet expectations;
- adverse developments in the worldwide economy, the financial markets, the engineering and consulting services market, the real estate market, the public works/infrastructure market, and/or the energy/ industrial market;
- changes in interest rates;
- our failure to meet securities analysts expectations;
- changes in accounting principles;
- sales of common stock by existing shareholders or holders of options;
- announcements of key developments by our competitors;
- the reaction of markets and securities analysts to announcements and developments involving our company; and
- resolution of threatened or pending litigation.

In the past, securities class action litigation has often been brought against a company following periods of volatility in the market price of its securities. We may in the future be the target of similar litigation. Securities litigation could result in substantial costs and divert management s attention and resources.

Insiders have substantial control over us, which could limit your ability to influence the outcome of key transactions

Our executive officers and directors, in the aggregate, hold approximately 17% of our outstanding common stock. These shareholders, if they act together, can have significant influence over most matters requiring approval by our shareholders, including the election of directors and the approval of mergers or other business combination transactions.

If we need to sell or issue additional shares of common stock and/or incur additional debt to finance future acquisitions, your stock ownership could be diluted and our results of operations could be adversely affected

Our business strategy is to expand into new markets and enhance our position in existing markets through the acquisitions of complementary businesses. In order to successfully complete targeted acquisitions or to fund our other activities, we may issue additional equity securities that could dilute your stock ownership. We may also incur additional debt if we acquire another company, and this could negatively impact our results of operations.

Our board of directors has the ability to discourage takeover attempts, which may reduce or eliminate your ability to sell your shares for a premium in a change of control transaction

Our amended and restated articles of incorporation provide us with the ability to issue blank check preferred stock without consulting our shareholders. As a result, our board of directors may frustrate a takeover attempt by issuing shares to a friendly shareholder or acquirer, implementing a poison pill or otherwise creating features of newly issued preferred stock.

Shares of our common stock eligible for public sale could cause the market price of our stock to drop, even if our business is doing well

We currently have approximately 7.7 million shares of common stock outstanding. Sales of a substantial number of shares of our common stock in the public market, or the perception that these sales could occur, could adversely affect the market price for our common stock. Certain shareholders hold large numbers of shares which they are able to sell in the public market. Significant sales of these shares could cause the market price of our common stock to decline regardless of the performance of our business. These sales also might make it difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate.

Our common stock is thinly traded. Consequently, it may be difficult for shareholders to sell our common stock, which may result in losses for investors

The average daily trading volume, excluding block trades, for our common stock on the Nasdaq National Market was approximately 14,000 shares from January 1, 2003 through December 31, 2003. Accordingly, the market price of our common stock is subject to significant fluctuations that may have been, and may continue to be, exaggerated due to the lack of an active trading market for our common stock. This negative factor may make it difficult for shareholders to sell the Company s common stock, which may result in losses for investors.

Item 7A. ***Quantitative and Qualitative Disclosures About Market Risk***

We are exposed to interest rate changes primarily as a result of our cash and cash equivalents (Cash), securities held-to-maturity (Securities) and line of credit, which are used to maintain liquidity and to fund capital expenditures and our expansion. Due to our large balance of Cash and Securities, our earnings and cash flows may be materially impacted by changes in interest rates. The Company intends to hold all of its Securities until maturity, and therefore, should not bear any interest rate risk due to early disposition. Due to the relatively immaterial levels of our current debt (which was zero as of December 31, 2003), our earnings and cash flows should not be materially impacted by changes in interest rates on our debt. Our bank line of credit is based on variable interest rates and is therefore affected by changes in market rates. We do not enter into derivative or interest rate hedging transactions.

The table below presents the principal amounts of Securities, along with the weighted average interest rates, fair values and expected maturity by year to evaluate the expected cash flows and sensitivity to interest rate changes as of December 31, 2003.

	2004	Fair Value(1)
Securities held-to-maturity (non-trading)	$4,600,000	$4,600,000
Weighted average interest rate(2)	1.16%	1.16%

(1) The fair value for Securities was based on the quoted market price of such securities as of December 31, 2003.

(2) The Company s Securities are invested in federally tax-exempt bonds. The weighted average interest rate shown above is a combination of pre-tax interest rate for taxable securities and an after tax interest rate for tax-exempt securities.

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As the table incorporates only those exposures that existed as of December 31, 2003, it does not consider those exposures or positions which could arise after that date. Moreover, because firm commitments are not presented in the table above, the information presented in the table has limited predictive value. Our ultimate realized gain or loss with respect to interest rate fluctuations will depend on those exposures or positions that arise during the period and interest rates.

Item 8. ***Consolidated Financial Statements and Supplementary Data***

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INDEPENDENT AUDITORS REPORT

The Board of Directors and Shareholders

The Keith Companies, Inc.:

We have audited the accompanying consolidated balance sheets of The Keith Companies, Inc. and subsidiaries as of December 31, 2002 and 2003, and the related consolidated statements of income, shareholders equity, and cash flows for each of the years in the three-year period ended December 31, 2003. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Keith Companies, Inc. and subsidiaries as of December 31, 2002 and 2003, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States of America.

/s/ KPMG LLP

Orange County, California
February 6, 2004

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	December 31,	
	2002	**2003**
ASSETS		
Current assets:		
Cash and cash equivalents	$20,333,000	$24,277,000
Securities held-to-maturity	3,164,000	4,600,000
Contracts and trade receivables, net of allowance for doubtful accounts of $1,123,000 and $1,328,000 at December 31, 2002 and 2003, respectively	18,771,000	19,844,000
Costs and estimated earnings in excess of billings	10,392,000	9,997,000
Prepaid expenses and other currents assets	1,367,000	1,468,000
Total current assets	54,027,000	60,186,000
Equipment and leasehold improvements, net	4,831,000	4,067,000
Goodwill, net of accumulated amortization of $761,000 at December 31, 2002 and 2003	23,056,000	23,059,000
Other assets	312,000	224,000
Total assets	$82,226,000	$87,536,000
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current portion of long-term debt and capital lease obligations	$ 52,000	$
Trade accounts payable	1,818,000	1,640,000
Accrued employee compensation	3,722,000	4,037,000
Current portion of deferred tax liabilities	3,065,000	2,444,000
Other accrued liabilities	4,484,000	3,078,000
Billings in excess of costs and estimated earnings	1,273,000	1,571,000
Total current liabilities	14,414,000	12,770,000
Long-term debt and capital lease obligations, less current portion	18,000	
Issuable common stock	2,215,000	792,000
Deferred tax liabilities	1,675,000	1,560,000
Accrued rent	292,000	452,000
Total liabilities	18,614,000	15,574,000
Shareholders equity:		
Preferred stock, $0.001 par value. Authorized 5,000,000 shares; no shares issued or outstanding		
Common stock, $0.001 par value. Authorized 100,000,000 shares ; issued and outstanding 7,514,140 and 7,653,935 shares in 2002 and 2003, respectively	8,000	8,000
Additional paid in capital	44,166,000	45,295,000
Retained earnings	19,438,000	26,659,000

Total shareholders equity	63,612,000	71,962,000
Commitments and contingencies (Notes 6, 9, 10, 17, and 18)		
Total liabilities and shareholders equity	$ 82,226,000	$ 87,536,000

See accompanying notes to consolidated financial statements.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

	Years Ended December 31,		
	2001	2002	2003
Gross revenue	$74,314,000	$106,487,000	$99,950,000
Subcontractor costs	7,470,000	14,889,000	9,206,000
Net revenue	66,844,000	91,598,000	90,744,000
Costs of revenue	42,970,000	59,716,000	58,837,000
Gross profit	23,874,000	31,882,000	31,907,000
Selling, general and administrative expenses	14,015,000	19,105,000	20,592,000
Income from operations	9,859,000	12,777,000	11,315,000
Interest income	552,000	384,000	279,000
Interest expense (income), net	263,000	(47,000)	15,000
Other expenses (income), net	54,000	(625,000)	(259,000)
Income before provision for income taxes and discontinued operations	10,094,000	13,833,000	11,838,000
Provision for income taxes	3,916,000	5,397,000	4,617,000
Income from continuing operations	6,178,000	8,436,000	7,221,000
Loss from discontinued operations, net of income taxes	329,000	628,000	
Net income	$ 5,849,000	$ 7,808,000	$ 7,221,000
Earnings per share from continuing operations:			
Basic	$ 0.94	$ 1.15	$ 0.95
Diluted	$ 0.87	$ 1.07	$ 0.91
Earnings (loss) per share from discontinued operations, net of income taxes:			
Basic	$ (0.05)	$ (0.09)	$
Diluted	$ (0.05)	$ (0.08)	$
Earnings per share:			
Basic	$ 0.89	$ 1.06	$ 0.95
Diluted	$ 0.82	$ 0.99	$ 0.91
Weighted average number of shares outstanding:			
Basic	6,604,367	7,363,073	7,615,264
Diluted	7,092,505	7,868,877	7,957,344

See accompanying notes to consolidated financial statements.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

Years Ended December 31, 2001, 2002 and 2003

	Shares Outstanding	Common Stock	Additional Paid-In Capital	Retained Earnings	Total
Balance at December 31, 2000	5,115,882	$5,000	$12,453,000	$ 5,781,000	$18,239,000
Issuance of common stock	1,970,093	2,000	28,601,000		28,603,000
Stock options exercised	278,709		596,000		596,000
Tax benefit from exercise of stock options			879,000		879,000
Net income				5,849,000	5,849,000
Repurchase of common stock	(55,000)		(433,000)		(433,000)
Balance at December 31, 2001	7,309,684	7,000	42,096,000	11,630,000	53,733,000
Issuance of common stock	174,783	1,000	1,822,000		1,823,000
Stock options exercised	29,673		159,000		159,000
Tax benefit from exercise of stock options			89,000		89,000
Net income				7,808,000	7,808,000
Balance at December 31, 2002	7,514,140	8,000	44,166,000	19,438,000	63,612,000
Issuance of common stock	70,907		714,000		714,000
Stock options exercised	68,888		309,000		309,000
Tax benefit from exercise of stock options			69,000		69,000
Deferred compensation			37,000		37,000
Net income				7,221,000	7,221,000
Balance at December 31, 2003	7,653,935	$8,000	$45,295,000	$26,659,000	$71,962,000

See accompanying notes to consolidated financial statements.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
	2001	**2002**	**2003**
Cash flows from operating activities:			
Net income	$ 5,849,000	$ 7,808,000	$ 7,221,000
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	2,349,000	2,283,000	2,231,000
Loss on sale/ impairment of equipment	23,000	93,000	29,000
Reduction in purchase price of acquired companies		(769,000)	(137,000)
Tax benefit from exercise of stock options	879,000	89,000	69,000
Stock compensation expense			37,000
Changes in operating assets and liabilities, net of effects from acquisitions:			
Contracts and trade receivables, net	659,000	3,369,000	(1,269,000)
Costs and estimated earnings in excess of billings	(1,807,000)	(1,545,000)	304,000
Prepaid expenses and other current assets	(366,000)	108,000	(53,000)
Trade accounts payable and accrued liabilities	277,000	(270,000)	(652,000)
Billings in excess of costs and estimated earnings	(341,000)	(1,042,000)	298,000
Deferred tax liabilities	306,000	(28,000)	(728,000)
Net cash provided by operating activities	7,828,000	10,096,000	7,350,000
Cash flows from investing activities:			
Net cash expended for acquisitions	(5,834,000)	(8,048,000)	(722,000)
Additions to equipment and leasehold improvements	(1,575,000)	(1,872,000)	(1,548,000)
Proceeds from (purchase of) securities held-to-maturity	(11,521,000)	8,357,000	(1,436,000)
Proceeds from sales of equipment	15,000	134,000	57,000
Net cash used in investing activities	(18,915,000)	(1,429,000)	(3,649,000)
Cash flows from financing activities:			
Payments on line of credit, net	(2,294,000)		
Principal payments on long-term debt and capital lease obligations, including current portion	(3,528,000)	(705,000)	(52,000)
Repurchase of common stock	(433,000)		
Proceeds from exercise of stock options	596,000	159,000	295,000
Net proceeds from stock offering	27,915,000		
Net cash provided by (used in) financing activities	22,256,000	(546,000)	243,000
Net increase in cash and cash equivalents	11,169,000	8,121,000	3,944,000
Cash and cash equivalents, beginning of year	1,043,000	12,212,000	20,333,000
Cash and cash equivalents, end of year	$ 12,212,000	$ 20,333,000	$ 24,277,000

See supplemental cash flow information at Note 15.

See accompanying notes to consolidated financial statements.

THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years Ended December 31, 2001, 2002, and 2003

(1) Organization and Basis of Presentation

The Keith Companies, Inc. (TKCI), is incorporated in the state of California and has been conducting business since 1983. TKCI is a full service engineering and consulting services firm providing professional services on a wide range of short and long-term projects pursuant to mainly short-term contracts to the real estate development and public works/infrastructure industry, and the energy/industrial industry. These services are rendered principally in California, Nevada, Utah, Arizona, Oregon, Texas, and Michigan. References to TKCI or the Company mean the Company and all of its wholly-owned subsidiaries.

The Company provides a full range of services from initial site acquisition studies through construction support services to clients operating in a variety of market sectors. The Company benefits from a diverse public and private client base including real estate developers, residential and commercial builders, architects, cities, counties, water districts, state and federal agencies, land owners, commercial retailers, energy providers and various manufacturers. The Company s professional staff provides a comprehensive menu of services that are needed to effectively manage, engineer and design infrastructure and state-of-the-art facilities.

(2) Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements of the Company are prepared in accordance with accounting principles generally accepted in the United States of America. All material intercompany transactions and balances have been eliminated in consolidation.

Cash and Cash Equivalents

Cash equivalents are primarily comprised of highly liquid debt instruments with maturities of three months or less when purchased. The Company s excess cash is managed by two financial institutions and, therefore, may be subject to certain concentration of credit risks.

Securities Held-to-Maturity

The Company accounts for its securities as held-to-maturity (Securities) under the provisions of Statement of Financial Accounting Standards (SFAS) No. 115, Accounting for Certain Investments in Debt and Equity Securities. Under SFAS No. 115, the Company is required to classify its Securities in one of three categories: trading, available-for-sale, or held-to-maturity. Trading securities are bought and held principally for the purpose of selling them in the near term. Held-to-maturity securities are those securities for which the Company has the intent and ability to hold until maturity. All other securities not included in trading or held-to-maturity categories are classified as available-for-sale. The Company has the ability and intent to hold all of its Securities until maturity and therefore, has classified its Securities as held-to-maturity. Accordingly, the Securities are stated at amortized cost. The Company s Securities are invested in highly liquid investment grade short-term debt securities.

Allowance for Doubtful Accounts

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability to collect on its contracts and trade receivables. The Company uses estimates in arriving at its allowance for doubtful accounts which are based on its best assessment as to the collectibility of the related receivable balance.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Revenue and Cost Recognition on Contracts

The Company enters into fixed fee contracts and contracts that provide for fees on a time-and-materials basis, most of which have not-to-exceed provisions. Contracts typically vary in length between six months and three years. However, many contracts are for small increments of work, which can be completed in less than six months. For contracts with a fixed fee or a not-to-exceed provision, revenue is recognized on the percentage of completion method of accounting based on the proportion of actual direct contract costs incurred to total estimated direct contract costs. Management considers costs incurred to be the best available measure of progress on contracts. For time and material contracts, revenue is recognized as earned.

In the course of providing its services, the Company sometimes subcontracts with various providers and professionals like technical consultants, product suppliers and installers, landscape architects, architects, geotechnical engineers, structural engineers, traffic engineers, and aerial photographers. These costs are included in the billings to the clients and are included in the Company s gross revenue. Because subcontractor services can change significantly from project to project, changes in gross revenue may not be indicative of business trends. Accordingly, the Company also reports net revenue, which is gross revenue less subcontractor costs.

Costs of revenue include labor, non-reimbursable costs, materials and various direct and indirect overhead costs including rent, utilities and depreciation. General and administrative costs are charged to expense as incurred. Provisions for estimated losses on uncompleted contracts are made in the period in which the losses are determined. Changes in job performance, job conditions and estimated profitability, including final contract settlements, may result in revisions to costs and income and are recognized in the period in which the revisions are determined. Additional revenue resulting from requests for additional work due to changes in the scope of engineering services to be rendered, are included in revenue when realization is probable and can be estimated with reasonable certainty.

Costs and estimated earnings in excess of billings represents revenue recognized in excess of amounts billed on the respective uncompleted engineering contracts. Billings in excess of costs and estimated earnings represents amounts billed in excess of revenue recognized on the respective uncompleted contracts.

At December 31, 2002 and 2003, the Company had no significant amounts included in contracts and trade receivables or trade accounts payable representing amounts retained pending contract or subcontractor completion.

Equipment and Leasehold Improvements

Equipment and leasehold improvements are stated at cost, while capital leased assets are stated at the lesser of the present value of future minimum lease payments or fair value. Depreciation/amortization is provided on a straight-line basis over the estimated useful lives of the assets, as follows:

Equipment	3 to 10 years
Leasehold improvements	1 to 7 years

When assets are sold or otherwise retired, the related cost and accumulated depreciation/amortization are removed from the accounts and the resulting gain or loss is included in other expenses (income), net in the accompanying consolidated statements of income.

Goodwill

Goodwill represents the excess of the purchase price over the estimated fair value of the tangible and intangible net assets acquired and liabilities assumed. Prior to the adoption of SFAS No. 142 Goodwill and Other Intangible Assets effective January 1, 2002, goodwill was being amortized over 25 years. Beginning

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

January 1, 2002, goodwill is no longer amortized and is required to be tested for impairment on an annual basis or more frequently if an event occurs or circumstances change that would indicate that the carrying amount may be impaired (see Note 5 Goodwill).

Income Taxes

The Company accounts for income taxes under the asset and liability method in accordance with SFAS No. 109, Accounting for Income Taxes, which requires recognition of deferred tax assets and liabilities for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The Company considers recording a valuation allowance to reflect the estimated amount of deferred tax assets which may not be realized. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Stock Option Plan

The Company accounts for its stock options and restricted shares in accordance with the provisions of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. The Company has not recorded any compensation expense related to the granting of stock options. The Company, however, has recorded compensation expense related to the granting of restricted shares in 2003 (see Note 10 Common Stock and Stock Plans). SFAS No. 123, Accounting for Stock Based Compensation, permits entities to recognize the fair value of all stock-based awards on the date of grant as an expense over the vesting period. Alternatively, SFAS No. 123 allows entities to continue to apply the provisions of APB Opinion No. 25; however, SFAS No. 148, Accounting for Stock Based Compensation Transition and Disclosure , requires pro forma net income disclosures as if the fair-value-based method defined in SFAS No. 123 had been applied. The Company has elected to continue to apply the provisions of APB Opinion No. 25 and to provide the pro forma disclosure specified by SFAS No. 148.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Had the Company determined compensation cost based on the fair value at the grant date for its stock options (using the Black-Scholes method) and restricted shares under SFAS No. 123, the Company s net income would have been adjusted to the pro forma amounts indicated below:

	Years Ended December 31,		
	2001	2002	2003
Net income:			
Net income, as reported	$5,849,000	$7,808,000	$7,221,000
Add: Employee compensation expense related to restricted shares, included in net income, net of taxes			23,000
Deduct: Stock-based employee compensation expense determined under the fair-value based method, net of taxes	(353,000)	(404,000)	(472,000)
Pro forma net income	$5,496,000	$7,404,000	$6,772,000
Basic earnings per share:			
As reported	$0.89	$1.06	$0.95
Pro forma	$0.83	$1.01	$0.89
Diluted earnings per share:			
As reported	$0.82	$0.99	$0.91
Pro forma	$0.77	$0.94	$0.85

The following represents assumptions used to estimate the fair value of stock options granted as determined using the Black-Scholes option pricing model:

	Years Ended December 31,		
	2001	2002	2003
Weighted average stock price per share of common stock at grant date	$7.69	$8.21	$8.76
Weighted average exercise price per stock option granted	$7.69	$8.21	$8.76
Expected volatility	76.2%	68.4%	61.8%
Risk-free interest rate	4.2%	2.7%	3.2%
Expected option term (years)	5	5	5
Stock dividend yield	0.0%	0.0%	0.0%

The weighted average fair value of stock options granted during the years ended December 2001, 2002, and 2003 was $8.91, $7.76, and $5.61 per share, respectively.

Earnings Per Share

Basic earnings per share (EPS) is computed by dividing net income during the period by the weighted average number of common shares outstanding during each period. Diluted EPS is computed by dividing net income during the period by the weighted average number of shares that would have been outstanding assuming the issuance of dilutive potential common shares as if outstanding during the reporting period, net of shares assumed to be repurchased using the treasury stock method.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following is a reconciliation of the denominator for the basic EPS computation to the denominator of the diluted EPS computation.

	Years Ended December 31,		
	2001	2002	2003
Weighted average shares used for the basic EPS computation	6,604,367	7,363,073	7,615,264
Incremental shares from the assumed exercise of dilutive stock options, restricted shares, stock warrants, and contingently issuable shares	488,138	505,804	342,080
Weighted average shares used for the diluted EPS computation	7,092,505	7,868,877	7,957,344

In conjunction with certain acquisitions, the Company agreed to pay consideration consisting of shares of its common stock (see Note 6). As a result, the Company estimated and included 169,989, 260,917 and 75,454 weighted average contingently issuable shares in its weighted average shares used for the diluted EPS computation for the years ended December 31, 2001, 2002 and 2003, respectively.

There were 84,959, 138,693 and 167,965 anti-dilutive weighted stock options excluded from the above calculation in 2001, 2002 and 2003, respectively.

Use of Estimates in the Preparation of Consolidated Financial Statements

The preparation of these consolidated financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the amounts of revenue and expenses reported during the periods. Actual results may differ from the estimates and assumptions used in preparing these consolidated financial statements.

Risks and Uncertainties

As of December 31, 2003, approximately 10% of the Company s work force is covered by collective bargaining agreements that expire during 2004 and 2005.

Reclassifications

Certain 2001 and 2002 balances have been reclassified to conform to the presentation used in 2003.

(3) Discontinued Operations

During 2002, the Company closed three of its divisions. Two of these divisions relate to the Company s acquisition of Hook & Associates Engineering, Inc. (Hook) and were located in Colorado and Wyoming. The third closure related to the Company s internally developed Communication division, which was located in California. The closures were primarily due to lower than expected operating results and continuing difficult market conditions. In accordance with accounting principles generally accepted in the United State of America (GAAP), the balances and activities of these divisions have been segregated and reported as discontinued operations for the current year and all prior years effected.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(4) Secondary Offering of Common Stock

Secondary Offering. In May 2001, the Company completed a secondary offering of an aggregate of 2.3 million shares of common stock (including an over-allotment of 300,000 shares), of which 1.9 million shares were sold by the Company and 400,000 shares were sold by selling shareholders. The public offering price was $16.00 per share, which resulted in proceeds to the Company, net of underwriting fees and offering expenses, of approximately $27.9 million.

The Company used a portion of the net proceeds from the secondary offering to repay debt, for general corporate purposes, including working capital and to aid in completing acquisitions. The remaining balance of the net proceeds has been invested in highly liquid investment grade short-term debt securities held to maturity.

(5) Goodwill

Effective January 1, 2002, the Company adopted SFAS No. 142. Under this standard, goodwill is no longer amortized. Therefore, no goodwill amortization expense was incurred during the years ended December 31, 2002 and 2003. Beginning January 1, 2002, goodwill is required to be tested for impairment on an annual basis, and is required to be tested for impairment between annual tests if an event occurs or circumstances change that would indicate the carrying amount may be impaired. The table below shows the as adjusted effect on net income, basic earnings per share and diluted earnings per share had SFAS No. 142, which eliminated goodwill amortization, been applied in 2001:

	Years Ended December 31,		
	2001	**2002**	**2003**
Net income:			
Reported net income	$5,849,000	$7,808,000	$7,221,000
Add back: Goodwill amortization (net of income taxes)	264,000		
Adjusted net income	$6,113,000	$7,808,000	$7,221,000
Basic earnings per share:			
Reported basic earnings per share	$ 0.89	$ 1.06	$ 0.95
Add back: Goodwill amortization (net of income taxes)	0.04		
Adjusted basic earnings per share	$ 0.93	$ 1.06	$ 0.95
Diluted earnings per share:			
Reported diluted earnings per share	$ 0.82	$ 0.99	$ 0.91
Add back: Goodwill amortization (net of income taxes)	0.04		
Adjusted diluted earnings per share	$ 0.86	$ 0.99	$ 0.91

For financial reporting purposes, the Company has grouped its operations into two primary reportable segments: Real Estate Development and Public Works/ Infrastructure (REPWI) and Energy/ Industrial (EI). The changes in the carrying amount of goodwill as reported by each reportable segment for the year ended December 31, 2003 is as follows:

	REPWI	EI	Total
Balance as of December 31, 2002	$18,191,000	$4,865,000	$23,056,000
Purchase price adjustments	(34,000)	37,000	3,000
Balance as of December 31, 2003	$18,157,000	$4,902,000	$23,059,000

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Consistent with the Company s policy, the Company performed its 2002 and 2003 annual goodwill impairment test during the fourth quarter of those years, which resulted in no changes in the carrying value of goodwill at December 31, 2002 and 2003.

(6) Acquisitions

ALNM Group, Inc.

Effective March 1, 2002, the Company acquired all the outstanding shares of common stock of ALNM Group, Inc. (ALNM) for an adjusted purchase price of $10.1 million. The results of ALNM s operations have been included in the consolidated financial statements since March 2002. ALNM, based in Michigan, specializes in government services, with expertise in environmental, civil, mechanical and electrical engineering as well as planning and surveying. The acquisition expanded TKCI s geographic coverage and enhanced TKCI s array of services it offers to clients in the public works and infrastructure industries. The adjusted purchase price consists of $7.7 million which was paid in cash and $2.4 million of the Company s common stock, of which $1,569,000 was issued in 2002 and an estimated $792,000 in value of shares is to be issued in 2004.

In accordance with SFAS No. 141, this acquisition was accounted for using the purchase method of accounting. Therefore, the Company recorded adjusted goodwill of $8,220,000, which represents the excess of the adjusted purchase price over the fair value of the net tangible and identifiable intangible assets acquired and liabilities assumed.

Universal Energy, Inc.

On November 30, 2001, the Company acquired all the outstanding shares of common stock of Universal Energy, Inc. (UEI) and its wholly owned subsidiary Amerex International, Inc. for an adjusted purchase price of $4.7 million. The results of UEI s operations have been included in the consolidated financial statements since December 2001. UEI, which is based in Texas, provides start-up management, technical support, facility acquisition analysis, operations and maintenance, and manpower augmentation to the power industry. This acquisition has enhanced TKCI s geographic coverage and has expanded TKCI s package of services it can offer to clients in the power and energy industries. The adjusted purchase price consists of $4.0 million which was paid in cash and $714,000 paid in the Company s common stock. In addition, the former shareholders may be eligible for additional consideration which may affect the purchase price as a result of an earn-out provision. Under the earn-out provision, the former shareholders may be eligible to receive future cash and stock payments based on certain profitability targets during 2004.

In accordance with SFAS No. 141, this acquisition was accounted for using the purchase method of accounting. Therefore, the Company recorded adjusted goodwill of $3,313,000, which represents the excess of the adjusted purchase price over the fair value of the net tangible and intangible assets acquired and liabilities assumed.

Pacific Engineering Corporation

On September 28, 2001, the Company acquired substantially all of the assets and assumed substantially all of the liabilities of Pacific Engineering Corporation (PEC) for an adjusted purchase price of $2,212,000, paid in cash. The results of PEC s operations have been included in the consolidated financial statements since October 2001. PEC is an Oregon based engineering and design services firm specializing in the fields of power transmission and distribution, hydroelectric energy facilities, and other utility infrastructure services. The acquisition has diversified TKCI geographically, as well as increased TKCI s service offerings through a new expertise in power transmission and hydroelectric power.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In accordance with SFAS No. 141, this acquisition was accounted for using the purchase method of accounting. Therefore, the Company recorded adjusted goodwill of $1,589,000, which represents the excess of the adjusted purchase price over the fair value of the net tangible and intangible assets acquired and liabilities assumed.

Hook & Associates Engineering, Inc.

On January 31, 2001, the Company acquired substantially all of the assets and assumed substantially all of the liabilities of Hook & Associates Engineering, Inc. (Hook) for an adjusted purchase price of $3,510,000. The adjusted purchase price reflects the reduction of consideration resulting from a modification agreement in July 2002, which resulted in the Company reducing goodwill, certain operating assets, and interest expense by $282,000, $178,000, and $130,000 respectively, and increasing other income by $379,000. The results of Hook s operations have been included in the consolidated financial statements since February 2001. This acquisition was accounted for using the purchase method of accounting. Accordingly, the Company recorded adjusted goodwill of $2,440,000, which represents the excess of the adjusted purchase price over the fair value of the net tangible and identifiable intangible assets acquired and liabilities assumed. Such amount was amortized over a period of 25 years through December 31, 2001.

(7) Equipment and Leasehold Improvements

Equipment and leasehold improvements at December 31, 2002 and 2003 consist of the following:

	2002	2003
Equipment	$12,815,000	$ 14,075,000
Leasehold improvements	613,000	544,000
Accumulated depreciation and amortization	(8,597,000)	(10,552,000)
Equipment and leasehold improvements, net	$ 4,831,000	$ 4,067,000

(8) Indebtedness

Line of Credit, Long-Term Debt and Capital Lease Obligations

	December 31, 2002	December 31, 2003
Capital lease obligations and other	70,000	
Less current portion	(52,000)	—
	$ 18,000	$

The Company has available a $10.0 million unsecured line of credit consisting of four components: (i) an acquisition component, (ii) an equipment and vehicle financing component, (iii) a standby letter of credit component, and (iv) a working capital component. The line provides up to a maximum of $5.0 million to finance acquisitions, up to a maximum of $3.0 million to finance equipment and vehicle purchases, up to a maximum of $1.0 million for standby letters of credit, and up to a maximum of $10.0 million less the aggregate outstanding principal balance of the acquisition, equipment and vehicle, and standby letter of credit components for working capital. The line bears interest at either a range of 0.25% below prime to prime, or a range of 1.25% to 1.75% over LIBOR depending on the Company s ability to meet certain financial covenants. All components of the line of credit mature in June 2005. This line of credit agreement restricts the payment of dividends without the bank s consent. As of December 31, 2003, the Company had utilized the letter of credit component of this line of credit to issue a $229,000 stand-by letter of credit. The Company did not have any outstanding balances under this line of credit agreement as of December 31, 2002.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(9) Leases

The Company has several noncancelable operating leases, primarily for office facilities, that expire through 2009. These facility leases generally contain renewal options for periods ranging from one to five years and require the Company to pay costs, including common area maintenance and insurance charges. Rental expense for operating leases during 2001, 2002 and 2003 totaled $3,109,000, $4,147,000 and $4,148,000, respectively.

Certain facilities have been subleased and also provide for reimbursement of various common area maintenance charges. Rental expense has been reduced for sublease income of $9,000, $233,000 and $335,000 for the years ended December 31, 2001, 2002 and 2003, respectively. Future minimum lease payments as of December 31, 2003 are as follows:

	Operating Leases
Years ending December 31:	
2004	$ 3,808,000
2005	3,519,000
2006	2,553,000
2007	1,512,000
2008	1,354,000
Thereafter	978,000
Total future minimum lease payments	$13,724,000

(10) Common Stock and Stock Plans

Stock Option Plan

In 1994, TKCI adopted a stock option plan (the Plan) under which common stock of TKCI was available for grant. The number of authorized shares to be granted under the Plan is 1,600,000. Under this plan, restricted shares may also be granted. Stock options have been granted with an exercise price equal to or greater than the stock s estimated fair market value at the date of grant. All stock options granted in connection with the Plan have a ten year term, vest and become exercisable ratably each year for a period of up to five years from the grant date. Stock option activity under the Plan during the periods indicated is as follows:

	Number of Stock Options	Weighted-Average Exercise Price
Balance at December 31, 2000	872,459	$ 5.51
Granted	181,650	14.03
Exercised	(189,959)	3.13
Forfeited	(66,338)	9.42
Balance at December 31, 2001	797,812	$ 7.69
Granted	115,500	13.27
Exercised	(29,673)	5.37
Forfeited	(44,161)	13.89

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Number of Stock Options	Weighted-Average Exercise Price
Balance at December 31, 2002	839,478	$ 8.21
Granted	154,500	10.03
Exercised	(68,888)	4.47
Forfeited	(54,886)	9.35
Balance at December 31, 2003	870,204	$ 8.76

The weighted average remaining contractual life and weighted average exercise price of stock options outstanding and exercisable as of December 31, 2003, were as follows:

	Outstanding			Exercisable	
Range of Exercise Prices	Number of Stock Options Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number of Stock Options Exercisable	Weighted Average Exercise Price
$2.70 to $5.12	244,383	4.61	$ 3.64	195,283	$ 3.36
$5.31 to $9.90	305,421	5.83	8.74	232,705	8.68
$10.01 to $22.00	320,400	8.60	12.68	52,860	15.11
	870,204	6.51	$ 8.76	480,848	$ 7.23

At December 31, 2001, 2002 and 2003, the number of shares of common stock subject to exercisable stock options were 296,328, 412,972 and 480,848, respectively, and the weighted-average exercise prices of those stock options were $5.54, $6.22 and $7.23, respectively.

In 2003, 20,000 restricted shares were granted to certain employees which vest over a 3 year period. The fair value of the restricted shares at the date of grant was $205,000. The deferred compensation of $205,000 is being expensed ratably over the vesting period to compensation expense and resulted in $23,000 of compensation expense, net of taxes, during 2003.

At December 31, 2003 there were 380,658 stock options and restricted shares available for grant under the Plan.

Stock Warrants

The Company issued stock warrants to purchase 150,000 shares of the Company s common stock in connection with the acquisitions of Thompson-Hysell, Inc., John M. Tettemer and Associates, Ltd., and ESI, Engineering Services Incorporated. Warrants were generally granted with an exercise price equal to or greater than the underlying stock s estimated fair market value at the date of grant, vested immediately and were exercisable at any time until the expiration date. All warrants were exercised as of December 31, 2001.

(11) Employee Benefit Plans

The Company has a defined contribution 401(k) plan covering a majority of its employees. This plan is designed to be tax deferred in accordance with the provisions of Section 401(k) of the Internal Revenue Code. Employees may contribute from 1% to 50%, subject to limitations, of compensation on a tax-deferred basis through a salary reduction arrangement. The Company s employer contribution is 100% of the first 3%, plus 50% of the next 2% of employee contributions, vesting immediately. During 2001, 2002 and 2003, the Company incurred $1,020,000, $1,444,000 and $1,423,000, respectively, related to its 401(k) plans, which represented the Company s entire obligations under the employer matching contribution program for the years ended December 31, 2001, 2002 and 2003.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(12) Income Taxes

The provision for income taxes consists of the following:

	Years Ended December 31,		
	2001	2002	2003
Current:			
Federal	$2,701,000	$3,738,000	$4,347,000
State	700,000	899,000	929,000
Foreign			77,000
Subtotal	3,401,000	4,637,000	5,353,000
Deferred:			
Federal	267,000	276,000	(608,000)
State	39,000	79,000	(128,000)
Subtotal	306,000	355,000	(736,000)
Total	$3,707,000	$4,992,000	$4,617,000
Provision for income taxes from continuing operations	$3,916,000	$5,397,000	$4,617,000
Provision (benefit) from discontinued operations	(209,000)	(405,000)	
Total provision for income taxes	$3,707,000	$4,992,000	$4,617,000

A reconciliation of income tax expense at the federal statutory rate of 34% to the Company s provision for income taxes is as follows:

	Years Ended December 31,		
	2001	2002	2003
Computed expected federal income tax expense	$3,432,000	$4,704,000	$4,025,000
State income tax expense, net of federal income tax benefit	513,000	699,000	533,000
Other	(29,000)	(6,000)	59,000
	$3,916,000	$5,397,000	$4,617,000

Current income tax expense does not reflect a $879,000, $89,000 and $69,000 tax benefit related to the exercise of employee stock options during 2001, 2002 and 2003, respectively. The tax benefit related to the exercise of employee stock options was recorded to additional paid-in capital in the accompanying consolidated statements of shareholders equity.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tax effects of temporary differences that give rise to significant portions of deferred tax assets and liabilities are as follows:

	December 31,	
	2002	2003
Deferred tax assets:		
Accrued liabilities and employee compensation	$ 401,000	$ 578,000
Billings in excess of costs and estimated earnings	497,000	613,000
Allowance for doubtful accounts	529,000	470,000
State tax	220,000	301,000
Other	267,000	190,000
Total deferred tax assets	1,914,000	2,152,000
Deferred tax liabilities:		
Equipment and improvements, net	363,000	270,000
Section 481, change from cash to accrual	1,175,000	692,000
Costs and estimated earnings in excess of billings	4,056,000	3,902,000
Goodwill amortization	584,000	833,000
Prepaid expenses	236,000	248,000
Other	240,000	211,000
Total deferred tax liabilities	6,654,000	6,156,000
Net deferred tax liabilities	$4,740,000	$4,004,000

The Company considers recording a valuation allowance in accordance with the provisions of SFAS No. 109 to reflect the estimated amount of deferred tax assets which may not be realized. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment, and believes it is more likely than not the Company will realize the benefits of its deferred tax assets.

As of December 31, 2003, the Company had no federal or state net operating loss carryforwards available to offset future taxable income.

(13) Segment and Related Information

The Company evaluates performance and makes resource allocation decisions based on the overall type of services provided to customers. For financial reporting purposes, the Company has grouped its operations into two reportable segments: Real Estate Development and Public Works/ Infrastructure (REPWI) and Energy/ Industrial (EI). The REPWI segment primarily provides engineering and consulting services for the development of both private projects (such as residential communities, commercial and industrial properties and recreational projects), and public works/ infrastructure projects (such as transportation and water/ sewage facilities). The EI segment provides the technical expertise and management required to design and test manufacturing facilities and processes and to facilitate the construction, through design, testing, and startup support of primary and alternate electrical power systems for power generators and large scale power consumers.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The acquisition of Hook in January 2001 and ALNM in March 2002 are reported as part of the Company s REPWI reporting segment, while the acquisition of PEC in September 2001 and UEI in November 2001 are reported as part of the Company s EI reporting segment.

The following tables set forth information regarding the Company s operating segments as of and for the years ended December 31, 2001, 2002 and 2003:

	Year Ended December 31, 2001			
	REPWI	EI	Corporate Costs	Consolidated
Net revenue	$60,069,000	$ 6,775,000	$	$66,844,000
Income from operations	$15,016,000	$ 1,271,000	$(6,428,000)	$ 9,859,000
Loss from discontinued operations	$ (538,000)	$	$	$ (538,000)
Identifiable assets	$58,994,000	$12,498,000	$	$71,492,000

	Year Ended December 31, 2002			
	REPWI	EI	Corporate Costs	Consolidated
Net revenue	$71,208,000	$20,390,000	$	$91,598,000
Income from operations	$16,560,000	$ 3,961,000	$(7,744,000)	$12,777,000
Loss from discontinued operations	$ (1,033,000)	$	$	$ (1,033,000)
Identifiable assets	$71,850,000	$10,376,000	$	$82,226,000

	Year Ended December 31, 2003			
	REPWI	EI	Corporate Costs	Consolidated
Net revenue	$78,430,000	$12,314,000	$	$90,744,000
Income from operations	$19,070,000	$ 827,000	$(8,582,000)	$11,315,000
Loss from discontinued operations	$	$	$	$
Identifiable assets	$78,342,000	$ 9,194,000	$	$87,536,000

Business Concentrations

In 2001, 2002 and 2003, the Company had no customers which represented greater than 10% of consolidated net revenue. No customers represented greater than 10% of net contract and trade receivables at December 31, 2002 and 2003.

(14) Fair Value of Financial Instruments

The carrying amounts of the Company s financial instruments reported in the accompanying consolidated balance sheets for cash and cash equivalents, securities held-to-maturity, contracts and trade receivables, costs and estimated earnings in excess of billings, trade accounts payable, accrued employee compensation, other accrued liabilities, and billings in excess of costs and estimated earnings approximate their fair values due to the short-term nature of these instruments.

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(15) Supplemental Cash Flow Information

	Years Ended December 31,		
	2001	2002	2003
Supplemental disclosure of cash flow information:			
Cash paid during the year for interest	$ 275,000	$ 34,000	$ 16,000
Cash paid during the year for income taxes	$1,661,000	$3,808,000	$6,152,000
Noncash financing and investing activities:			
Purchase price adjustment to issuable common stock	$	$ 715,000	$ 708,000
Cancellation of note payable	$	$1,300,000	$
Purchase price adjustment to other accrued liabilities	$	$ 890,000	$
Cancellation of issuable common stock	$	$1,490,000	$
Issuable common stock issued	$ 688,000	$1,822,000	$ 714,000

The initial purchase price allocation related to the acquisitions of Hook, PEC and UEI in 2001 and ALNM in 2002 resulted in the following increases:

	2001	2002
Contracts and trade receivables	$(7,187,000)	$(3,208,000)
Costs and estimated earnings in excess of billings	(129,000)	(843,000)
Prepaid expenses and other current assets	(34,000)	(124,000)
Goodwill	(6,479,000)	(8,421,000)
Equipment and leasehold improvements	(745,000)	(492,000)
Other assets	(116,000)	(87,000)
Line of credit	269,000	
Billings in excess of costs and estimated earnings	1,723,000	
Long-term debt, including current portion	1,720,000	
Accounts payable, accrued expenses and other liabilities	3,210,000	1,046,000
Deferred tax liabilities	734,000	1,532,000
Issuable common stock	1,200,000	3,300,000
Net initial cash expended for acquisitions	$(5,834,000)	$(7,297,000)
Additional cash expended during the year for previous acquisitions		(751,000)

Cash expended for acquisitions	$ (5,834,000)	$ (8,048,000)

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(16) Valuation and Qualifying Accounts

For the years ending December 31, 2001, 2002 and 2003, the following is supplementary information regarding valuation and qualifying accounts:

	Balance at Beginning of Period	Provision for Doubtful Accounts	Deductions	Balance at End of Period
Allowance for doubtful accounts:				
2001	$1,166,000	$(112,000)	$(103,000)	$ 951,000
2002	$ 951,000	$ 467,000	$(295,000)	$1,123,000
2003	$1,123,000	$ 483,000	$(278,000)	$1,328,000

(17) Commitments and Contingencies

The Company is also involved in various legal proceedings that arise in the ordinary course of business. Based on the Company s experience, the nature of our current proceedings and our insurance coverage for such matters, the ultimate disposition of these matters should not have a material adverse effect on the Company s financial position, liquidity or results of operations.

(18) Related Parties

The Company entered into change in control agreements with Aram H. Keith, our chief executive officer and chairman of the board, Eric C. Nielsen, our president and chief operating officer, and Gary C. Campanaro, our chief financial officer, secretary and a director of our company. These agreements provide that if the executive officer s employment with us terminates as a result of an involuntary or constructive termination (as these terms are defined in the agreements) at any time within two years following a change in control, then, in addition to other benefits, the executive officer will receive a one-time payment, equal to two times the executive officer s highest annual level of total cash compensation (including any and all bonus amounts) paid by us to that executive officer during any one of the three consecutive calendar years (inclusive of the year of termination) immediately prior to termination. The executive officer also is entitled to receive a payment by us to offset any excise tax under the Internal Revenue Code of 1986, as amended, that has been levied against the executive officer for payments that we have made to him. In addition, any unvested options previously granted to the executive officer will immediately vest and become exercisable as of the date of termination and remain exercisable until their respective expiration dates.

(19) Supplementary Financial Information (Unaudited)

The following is unaudited supplementary financial information for 2002 and 2003:

	For the Quarters Ended 2002			
	March 31,	June 30,	September 30,	December 31,
Net revenue	$20,803,000	$23,651,000	$24,810,000	$22,334,000
Gross profit	7,111,000	8,015,000	9,019,000	7,737,000
Income from continuing operations	1,544,000	2,071,000	3,024,000	1,797,000
Loss from discontinued operations	105,000	193,000	233,000	97,000
Net income	1,439,000	1,878,000	2,791,000	1,700,000

Basic earning per share from continuing operations	$	0.21	$	0.28	$	0.41	$	0.24

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THE KEITH COMPANIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	For the Quarters Ended 2003			
	March 31,	June 30,	September 30,	December 31,
Net revenue	$22,346,000	$22,777,000	$22,854,000	$22,767,000
Gross profit	7,404,000	7,788,000	8,485,000	8,230,000
Income from continuing operations	1,398,000	1,729,000	2,203,000	1,891,000
Net income	1,398,000	1,729,000	2,203,000	1,891,000
Basic earnings per share from continuing operations	$ 0.18	$ 0.23	$ 0.29	$ 0.25

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Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***

We have had no disagreements on accounting or financial disclosure matters with our independent auditors.

Item 9A. ***Controls and Procedures***

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms, and that such information is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure. As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures are effective in timely alerting them to material information required to be included in our periodic SEC reports.

In accordance with SEC requirements, our chief executive officer and chief financial officer note that, since the date of the most recent evaluation of our disclosure controls and procedures to the date of our Annual Report on Form 10-K, there have been no significant changes in our internal controls or in other factors that could significantly affect internal controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

Our management, including the chief executive officer and our chief financial officer, does not expect that our disclosure controls or our internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgements in decision-making can be faulty and that breakdowns can occur because of simple errors or mistakes. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART III

The information required by Items 10 through 14 of this report is set forth in the sections entitled Directors and Executive Officers, Executive Compensation, Security Ownership of Certain Beneficial Owners and Management, Certain Relationships and Related Transactions, and Principal Accountant Fees and Services in our Proxy Statement for our 2004 Annual Meeting of Shareholders. That information is incorporated in this Report and made a part hereof by reference.

PART IV

Item 15. ***Exhibits, Financial Statement Schedules and Reports on Form 8-K***

(a) The following documents are filed as part of this report:

(1) Consolidated Financial Statements.

The following Consolidated Financial Statements and the Independent Auditors Report are on pages 34 through 54 hereof:

Independent Auditors Reports.

Consolidated Balance Sheets as of December 31, 2002 and 2003

Consolidated Statements of Income for the years ended December 31, 2001, 2002 and 2003

Consolidated Statements of Shareholders Equity for the years ended December 31, 2001, 2002 and 2003

Consolidated Statements of Cash Flows for the years ended December 31, 2001, 2002 and 2003

Notes to Consolidated Financial Statements

(2) Financial Statement Schedules.

All Financial Statement Schedules have been omitted because they are not applicable or because the applicable disclosures have been included in the Consolidated Financial Statements or in the Notes thereto.

(3) Exhibits.

Exhibit Number	Description
3.1	Amended and Restated Articles of Incorporation of the registrant (incorporated herein by this reference to Exhibit 3.1 to the registrant s registration statement of Form S-1, registration number 333-77273).
3.2	Amended and Restated Bylaws of the registrant (incorporated herein by this reference to Exhibit 3.1 to the registrant s quarterly report on Form 10-Q for the period ended June 30, 2001).
4.1	Amended and Restated 1994 Stock Incentive Plan (incorporated herein by this reference to Exhibit 4.1 to the registrant s registration statement on Form S-8, registration Number 333-61312).
10.14	Severance Agreement between the registrant and Aram H. Keith (incorporated herein by this reference to Exhibit 10.14 to the registrant s annual report on Form 10-K for the period ended December 31, 2001).
10.15	Severance Agreement between the registrant and Eric C. Nielsen (incorporated herein by this reference to Exhibit 10.15 to the registrant s annual report on Form 10-K for the period ended December 31, 2001).
10.16	Severance Agreement between the registrant and Gary C. Campanaro (incorporated herein by this reference to Exhibit 10.16 to the registrant s annual report on Form 10-K for the period ended December 31, 2001).
10.17	Fourth Amendment to Credit Agreement dated January 31, 2001 by and between the Registrant, HEA Acquisition, Inc. and Wells Fargo Bank, National Association (incorporated herein by this reference to Exhibit 10.17 to the registrant s quarterly report on Form 10-Q for the period ended June 30, 2001).
10.18	Fifth Amendment to Credit Agreement dated April 27, 2001 by and between the Registrant, HEA Acquisition, Inc. and Wells Fargo Bank, National Association (incorporated herein by this reference to Exhibit 10.18 to the registrant s quarterly report on Form 10-Q for the period ended June 30, 2001).

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Exhibit Number	Description
10.19	Credit Agreement dated September 4, 2001 by and between the Registrant and Wells Fargo Bank, National Association (incorporated herein by this reference to Exhibit 10.19 to the registrant s quarterly report on Form 10-Q for the period ended September 30, 2001).
10.20	Line of Credit Note dated September 4, 2001 by and between the Registrant and Wells Fargo Bank, National Association (incorporated herein by this reference to Exhibit 10.20 to the registrant s quarterly report on Form 10-Q for the period ended September 30, 2001).
10.21	Third Amendment to Credit Agreement Dated September 4, 2001 by and between the Registrant and Wells Fargo Bank, National Association
21.0	List of Subsidiaries*
23.1	Consent of Independent Auditors*
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 Dated March 8, 2004
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 Dated March 8, 2004
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 Dated March 8, 2004
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 Dated March 8, 2004

* Filed herewith.

(b) Reports on Form 8-K.

On November 6, 2003 we filed a Current Report on Form 8-K, Items 5 and 12, relating to a press release announcing 2003 Third Quarter Results and Earnings Guidance.

On February 12, 2004, we filed a Current Report on Form 8-K, Items 5 and 12, relating to a press release announcing 2003 Year End Results and Earnings Guidance.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, The Keith Companies, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE KEITH COMPANIES, INC.

By: /s/ ARAM H. KEITH

Aram H. Keith
Chief Executive Officer

March 8, 2004

KNOWN BY ALL MEN THESE PRESENTS, that each person whose signature appears below constitutes and appoints Aram H. Keith and Gary C. Campanaro, or any one of them, his attorney-in-fact and agents with full power of substitution and re-substitution, for him and his name, place and stead, in any and all capacities, to sign any or all amendments to this Form 10-K and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the foregoing, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents, or either of them, or their substitutes, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following on behalf of The Keith Companies, Inc. and in the capacities and on the date indicated.

Signature	Title	Date
/s/ ARAM H. KEITH Aram H. Keith	Chief Executive Officer, Chairman of the Board and Director *(Principal Executive Officer)*	March 8, 2004
/s/ GARY C. CAMPANARO Gary C. Campanaro	Chief Financial Officer, Secretary and Director *(Principal Financial and Accounting Officer)*	March 8, 2004
/s/ GEORGE DEUKMEJIAN George Deukmejian	Director	March 8, 2004
/s/ CHRISTINE D. IGER Christine D. Iger	Director	March 8, 2004
/s/ EDWARD R. MULLER Edward R. Muller	Director	March 8, 2004

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