

Omega Flex, Inc.  
Form 10-Q  
May 08, 2009  
UNITED STATES

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended **March 31, 2009**

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number **000-51372**

**Omega Flex, Inc.**

(Exact name of registrant as specified in its charter)

**Pennsylvania**  
(State or other jurisdiction of incorporation or organization)  
**451 Creamery Way, Exton, PA**  
(Address of principal executive offices)

**23-1948942**  
(I.R.S. Employer Identification No.)  
**19341**  
(Zip Code)

**(610) 524-7272**

Registrant's telephone number, including area code

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, non-accelerated filer, or a smaller reporting company filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of The Exchange Act).

Yes  No

**APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS**

**DURING THE PRECEDING FIVE YEARS.**

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 12 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by the courts.

The number of shares of the registrant's common stock issued and outstanding as of April 30, 2009 was 10,091,822.

OMEGA FLEX, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR THE THREE MONTHS ENDED MARCH 31, 2009

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**PART I - FINANCIAL INFORMATION****Item 1 - Financial Statements****OMEGA FLEX, INC.****CONSOLIDATED BALANCE SHEETS****(unaudited)**

	<b><u>March 31,</u></b> <b><u>2009</u></b>	<b><u>December 31,</u></b> <b><u>2008</u></b>
	<b>(Dollars in thousands)</b>	
<b>ASSETS</b>		
Current Assets		
Cash and Cash Equivalents	\$ 8,917	\$9,773
Accounts Receivable - less allowances of \$51 and \$137, respectively	6,061	6,986
Inventories	8,165	10,242
Other Current Assets	<u>1,159</u>	<u>1,525</u>
Total Current Assets	<u>24,302</u>	<u>28,526</u>
Property and Equipment - net	6,590	6,407
Goodwill	3,526	3,526
Other Long-Term Assets	<u>526</u>	<u>534</u>
Total Assets	<u>\$34,944</u> =====	<u>\$38,993</u> =====
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts Payable	\$803	\$1,562
Accrued Compensation	197	2,169
Accrued Commissions & Sales Incentives	1,177	2,028
Other Liabilities	<u>855</u>	<u>1,657</u>
Total Current Liabilities	3,032	7,416
Deferred Taxes	1,182	1,168
Other Long-Term Liabilities	<u>1,034</u>	<u>1,025</u>
Total Liabilities	<u>5,248</u>	<u>9,609</u>
Equity:		
Omega Flex, Inc. Shareholders Equity:		
Common Stock par value \$0.01 Share: authorized 20,000,000 Shares: 10,091,822 and 10,093,808 shares issued and outstanding at March 31, 2009 and December 31, 2008, respectively	102	102
Paid in Capital	10,808	10,832
Retained Earnings	19,378	18,986
Accumulated Other Comprehensive Loss	<u>(721)</u>	<u>(672)</u>
Total Omega Flex, Inc. Shareholders Equity	<u>29,567</u>	<u>29,248</u>
Noncontrolling Interest	<u>129</u>	<u>136</u>
Total Shareholders Equity	<u>29,696</u>	<u>29,384</u>
Total Liabilities and Shareholders Equity	<u>\$34,944</u>	<u>\$38,993</u>

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See Accompanying Notes to Consolidated Financial Statements.

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## OMEGA FLEX, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

	<b>For the three-months ended March 31,</b>	
	<b><u>2009</u></b>	<b><u>2008</u></b>
	<b>(Amounts in thousands, except earnings per Common Share)</b>	
Net Sales	\$10,093	\$16,423
Cost of Goods Sold	<u>5,765</u>	<u>8,243</u>
Gross Profit	4,328	8,180
Selling Expense	1,994	2,494
General and Administrative Expense	1,163	1,891
Engineering Expense	<u>549</u>	<u>603</u>
Operating Profit	622	3,192
Interest Income, Net	19	102
Other Income (Expense), Net	<u>(10)</u>	<u>25</u>
Income Before Income Taxes	631	3,319
Income Tax Expense	<u>246</u>	<u>1,237</u>
Net Income	\$385	\$2,082
Less: Net (Income) Loss attributable to the Noncontrolling Interest	<u>7</u>	<u>(13)</u>
Net Income attributable to Omega Flex, Inc.	\$392	\$2,069
	===	=====
Basic Earnings per Common Share:		
Net Income	\$0.04	\$0.21
Basic Weighted Average Shares Outstanding	10,093	10,113
Diluted Earnings per Common Share:		
Net Income	\$0.04	\$0.21
Diluted Weighted Average Shares Outstanding	10,093	10,113

See Accompanying Notes to Consolidated Financial Statements.



## OMEGA FLEX, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

## For the three-months ended

	<b>March 31,</b>	
	<b><u>2009</u></b>	<b><u>2008</u></b>
	<b>(Dollars in thousands)</b>	
Cash Flows from Operating Activities:		
Net Income	\$392	\$2,069
Adjustments to Reconcile Net Income to		
Net Cash Used In Operating Activities:		
Depreciation and Amortization	116	146
Non-Cash Compensation Expense	7	15
Provision for Losses on Accounts Receivable, net of write-offs and recoveries	(8)	---
Change in Noncontrolling Interest	(7)	13
Changes in Assets and Liabilities:		
Accounts Receivable	923	617
Inventory	2,051	220
Accounts Payable	(1,822)	(199)
Accrued Compensation	(1,972)	(1,821)
Accrued Legal Settlement and Related Costs	(14)	(2,019)
Other Liabilities	(113)	(844)
Other Assets	<u>(44)</u>	<u>106</u>
Net Cash Used In Operating Activities	<u>(491)</u>	<u>(1,697)</u>
Cash Flows from Investing Activities:		
Capital Expenditures	<u>(313)</u>	<u>(102)</u>
Net Cash Used in Investing Activities	<u>(313)</u>	<u>(102)</u>
Cash Flows from Financing Activities:		
Treasury Stock Purchase	(24)	(340)
Dividends Paid	<u>---</u>	<u>(7,092)</u>
Net Cash Used in Financing Activities	<u>(24)</u>	<u>(7,432)</u>
Net Decrease in Cash and Cash Equivalents	(828)	(9,231)
Translation effect on cash	(28)	12
Cash and Cash Equivalents Beginning of Period	<u>9,773</u>	<u>13,143</u>
Cash and Cash Equivalents End of Period	<u>\$8,917</u>	<u>\$3,924</u>
	=====	=====

See Accompanying Notes to Consolidated Financial Statements.



OMEGA FLEX, INC.

**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(All dollars in thousands except per share amounts)

(Unaudited)

**1. BASIS OF PRESENTATION AND DESCRIPTION OF BUSINESS**

**Basis of Presentation**

The accompanying consolidated financial statements include the accounts of Omega Flex, Inc. (Omega) and its subsidiaries (collectively the Company). The Company's unaudited consolidated financial statements for the quarter ended March 31, 2009 have been prepared in accordance with generally accepted accounting principles, and with the instructions of Form 10-Q and Article 10 of Regulation S-X. All material inter-company accounts and transactions have been eliminated in consolidation. It is Management's opinion that all adjustments necessary for a fair statement of the results for the interim periods have been made, and that all adjustments are of a normal recurring nature or a description is provided for any adjustments that are not of a normal recurring nature.

**Description of Business**

The Company is a leading manufacturer of flexible metal hose, which is used in a variety of applications to carry gases and liquids within their particular applications. These applications include carrying liquefied gases in certain processing applications, fuel gases within residential and commercial buildings and vibration absorbers in high vibration applications. Our industrial flexible metal piping is used to carry other types of gases and fluids in a number of industrial applications where the customer requires the piping to have both a degree of flexibility and/or an ability to carry corrosive compounds or mixtures, or to carry at both very high and very low (cryogenic) temperatures.

The Company manufactures flexible metal hose at its facility in Exton, Pennsylvania, with a minor amount of manufacturing performed in the UK, and sells its product through distributors, wholesalers and to original equipment manufacturers (OEMs) throughout North America, and in certain European markets.

**Accounting Changes**

In December 2007, the FASB issued Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements - an amendment of ARB No. 51* (FAS 160), FAS 160 establishes and provides accounting and reporting standards for the noncontrolling interest in a consolidated subsidiary and for the deconsolidation of a subsidiary. The Company has adopted FAS 160 beginning January 1, 2009 via retrospective application of the presentation and disclosure requirements.



## 2. SIGNIFICANT ACCOUNTING POLICIES

### Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The most significant estimates and assumptions relate to revenue recognition and related sales incentives, accounts receivable valuations, inventory valuations, goodwill valuation, and accounting for income taxes. Actual amounts could differ significantly from these estimates.

### Revenue Recognition

The Company's revenue recognition activities relate almost entirely to the manufacture and sale of flexible metal hose and pipe. Under generally accepted accounting principles, revenues are considered to have been earned when the Company has substantially accomplished what it must do to be entitled to the benefits represented by the revenues. The following criteria represent preconditions to the recognition of revenue:

Persuasive evidence of an arrangement for the sale of product or services must exist.

Delivery has occurred or services rendered.

The sales price to the customer is fixed or determinable.

Collection is reasonably assured.

The Company generally recognizes revenue upon shipment in accordance with the above principles.

Gross sales are reduced for all consideration paid to customers for which no identifiable benefit is received by the Company. This includes promotional incentives, year end rebates, and discounts. The amounts of certain incentives are estimated at the time of sale.

Commissions, for which the Company receives an identifiable benefit, are accounted for as a sales expense.

### Earnings per Common Share

Basic earnings per share have been computed using the weighted average number of common shares outstanding. For the periods presented, there are no dilutive securities. Consequently, basic and dilutive earnings per share are the same.

**Currency Translation**

Assets and liabilities denominated in foreign currencies are translated into U.S. dollars at

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exchange rates prevailing on the balance sheet date. The Statement of Operations is translated into U.S. dollars at average exchange rates. Adjustments resulting from the translation of financial statements are excluded from the determination of income and are accumulated in a separate component of shareholders' equity. Exchange gains and losses resulting from foreign currency transactions are included in operations (other income (expense)) in the period in which they occur.

### **Income Taxes**

The Company accounts for federal tax liabilities in accordance with SFAS No. 109, Accounting for Income Taxes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. 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 effect on deferred tax assets and liabilities from a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided for deferred tax assets if it is more likely than not that these items will either expire before the Company is able to realize the benefit, or that future deductibility is uncertain.

### **Other Comprehensive (Loss) Income**

For the quarters ended March 31, 2009 and 2008, respectively, the components of Other Comprehensive (Loss) Income consisted solely of foreign currency translation adjustments.

### **Reclassifications**

Certain reclassifications have been made to prior years' financial statements to conform to the 2009 presentation.

### **3. INVENTORIES**

Inventories consisted of the following:

	<b>March 31, <u>2009</u> (unaudited) (dollars in thousands)</b>	<b>December 31, <u>2008</u></b>
Finished Goods	\$5,786	\$7,673
Raw Materials	<u>.379</u>	<u>2,569</u>
Total Inventory	\$8,165 =====	\$10,242 =====

### **4. SHAREHOLDERS' EQUITY**

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(Amounts in thousands, except share amounts)

As of March 31, 2009 and December 31, 2008, the Company had authorized 20,000,000 common stock shares with par value of \$0.01 per share, and had 10,091,822 and 10,093,808 shares issued and outstanding, respectively.

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On December 11, 2007, the Board authorized a special dividend of \$0.70 per share to all Shareholders of record as of January 3, 2008, which was subsequently paid on January 16, 2008

in the amount of \$7,092. In addition, on December 11, 2008, the Company announced that on December 8, 2008 the Board declared a dividend of \$0.50 per share to all shareholders of record as of December 16, 2008, which was paid on December 23, 2008 in the amount of \$5,047.

On September 12, 2007, the Company announced that its Board of Directors has authorized the purchase of up to \$5,000 of its common stock. The purchases may be made from time-to-time in open market or in privately negotiated transactions, depending on market and business conditions, within the next 24 months. The Board retained the right to cancel, extend, or expand the share buyback program, at any time and from time-to-time. During 2009, the Company purchased 1,986 shares for \$24, including commissions. Since inception, the Company has purchased a total of 61,811 shares for approximately \$932 or \$15 per share.

In connection with the aforementioned share buyback program, the Company has entered into a Rule 10b5-1 Repurchase Plan (the Plan) as of September 15, 2008 with Hunter Associates, Inc. ( Hunter ), by which Hunter will continue to implement the share buyback program by purchasing shares of the Company's common stock in accordance with the terms of the Plan and within the safe harbor afforded by Rule 10b5-1.

### 5. COMMITMENTS AND CONTINGENCIES

#### Commitments:

Under a number of indemnity agreements between the Company and each of its officers and directors, the Company has agreed to indemnify each of its officers and directors against any liability asserted against them in their capacity as an officer or director, or both. The Company's indemnity obligations under the indemnity agreements are subject to certain conditions and limitations set forth in each of the agreements. Under the terms of the Agreement, the Company is contingently liable for costs which may be incurred by the officers and directors in connection with claims arising by reason of these individuals' roles as officers and directors.

The Company has entered into salary continuation agreements with two employees, which provide for monthly payments to each of the employee or his designated beneficiary upon the employee's retirement or death. The payment benefits range from \$1 per month to \$3 per month with the term of such payments limited to 15 years after the employee's retirement at age 65. The agreements also provide for survivorship benefits if the employee dies before attaining age 65, and severance payments if the employee is terminated without cause, the amount of which is dependent on the length of company service at the date of termination. The net present value of the retirement payments is included in Other Long-Term Liabilities, which amounts to \$351 for March 31, 2009 and \$350 December 31, 2008, respectively. The Company has obtained and is the beneficiary of three whole life insurance policies in respect of the two employees discussed above, and one other policy. The cash surrender value of such policies (included in Other Assets) amounts to \$526 at March 31, 2009 and \$534 at December 31, 2008, respectively.

**Contingencies:**

The Company retains significant obligations under its commercial insurance policies for losses occurring in the policy years in which it was a subsidiary of Mestek, Inc. For the policy year ending October 1, 2004, the Company retained liability for the first \$2,000 per occurrence of commercial general liability claims (including product liability claims), subject to an agreed aggregate. In addition, for 2004 the Company retained liability for the first \$250 per occurrence of workers compensation coverage, subject to an agreed aggregate. However, for policy years beginning on July 22, 2005 (the effective date of the Spin-Off), the Company retained liability for a maximum of \$50 per occurrence of commercial liability claims (including products liability claims), subject to an agreed aggregate, and the Company is insured on a first dollar basis for workers' compensation subject to statutory limits.

As disclosed in the Company's December 31, 2008 Form 10-K, in October 2007, the Company entered into a subordination agreement with Bank of America (BOA), which is the main banking institution used by Omega's former parent Mestek, Inc. (Mestek), whereby the Company agreed to subordinate its loan to BOA's outstanding loans to Mestek. On July 31, 2008, Mestek paid the entire \$3,250 principal balance of the note with accrued interest to the Company in accordance with the terms of the note. The Company has subsequently received correspondence from attorneys for Bank of America that BOA believes the payment by Mestek to Omega Flex did not conform to the notice requirements of the subordination agreement, and have requested that the Company reinstitute the \$3,250 loan to Mestek, and to subordinate that loan to the BOA loan. The Company has reviewed this matter with outside counsel, and although we do not believe in light of all the facts that the Bank's position has any substantial merit, the board has authorized management to negotiate and enter into a new subordinated loan arrangement with BOA and Mestek with a maturity date in October 2010, and on other terms advantageous to the Company.

The Company's liability related to health insurance is limited to \$35 per case and an aggregate of \$660 annually.

**Warranty Commitments:**

Gas transmission products such as those made by the Company carry potentially serious personal injury risks in the event of failures in the field. As a result, the Company has extensive internal testing and other quality control procedures and historically the Company has not had a meaningful failure rate in the field due to the extensive nature of these quality controls. Due to the Company's quality systems, the warranty expense is *de minimis*, and accordingly, the Company does not maintain a warranty reserve beyond a nominal amount.

**6. STOCK BASED PLANS**

**Phantom Stock Plan**

**Plan Description.** On April 1, 2006, the Company adopted the Omega Flex, Inc. 2006 Phantom Stock Plan (the Plan). The Plan authorizes the grant of up to one million units of phantom stock to employees, officers or directors of the Company and of any of its subsidiaries.





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The phantom stock units ("Units") each represent a contractual right to payment of compensation in the future based on the market value of the Company's common stock. The Units are not shares of the Company's common stock, and a recipient of the Units does not receive any of the following:

- § ownership interest in the Company
- § shareholder voting rights
- § dividends or distributions
- § other incidents of ownership to the Company's common stock

The Units are granted to participants upon the recommendation of the Company's CEO, and the approval of the compensation committee. Each of the Units that are granted to a participant will be initially valued by the compensation committee, and at a minimum, the Unit's value will be in an amount equal to the closing price of the Company's common stock on the grant date. The Units follow a vesting schedule, with a maximum vesting schedule of 3 years after the grant date. Upon vesting, the Units represent a contractual right to the payment of the value of the Unit. The Units will be paid on their maturity date, which is a maximum of one year after all of the Units granted in a particular award have fully vested.

The amount to be paid to the participant on the maturity date is dependant on the type of Unit granted to the participant. The Units may be *Full Value*, in which the value of each Unit at the maturity date, will equal the closing price of the Company's common stock as of the maturity date; or *Appreciation Only*, in which the value of each Unit at the maturity date will be equal to the closing price of the Company's common stock at the maturity date *minus* the closing price of the Company's common stock at the grant date.

In certain circumstances, the Units may be immediately vested upon the participant's death or disability. All Units granted to a participant are forfeited if the participant is terminated from his relationship with the Company or its subsidiary for *cause*, which is defined under the

Plan. If a participant's employment or relationship with the Company is terminated for reasons other than for *cause*, then any vested Units will be paid to the participant upon termination. However, Units granted to certain specified employees as defined in Section 409A of the Internal Revenue Code will be paid approximately 181 days after that termination.

**Grants of Phantom Stock Units.** As of December 31, 2008, the Company had 6,892 units outstanding, all of which were granted at *Full Value*. On February 20, 2009, the Company granted an additional 8,645 *Full Value* Units with a face value of \$135 (fair value at grant date of approximately \$126). In all cases, the grant price was equal to the closing price of the Company's common stock at the grant date.

The Company uses the Black-Scholes option pricing model as its method for determining fair value of the Units. The Company uses the straight-line method of attributing the value of the stock-based compensation expense relating to the Units. The compensation expense (including adjustment of the liability to its fair value) from the Units is recognized over the service or vesting period of each grant or award.

Statement 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates in order to derive the Company's best estimate of awards ultimately to vest. Forfeitures represent only the

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unvested portion of a surrendered Unit and are typically estimated based on historical experience. As of October 8, 2007, in connection with an officer's resignation, a total of 2,874 unvested units were forfeited, however; based on an analysis of the Company's historical data, which has limited experience related to any stock-based plan forfeitures, the Company applied a 0% forfeiture rate to Plan Units outstanding in determining its Plan Unit compensation expense for March 31, 2009.

In accordance with SFAS 123R, the Company recorded compensation expense of approximately \$7 in 2009 related to the Phantom Stock Plan.

The fair value of the Units granted through the first quarter March 31, 2009 using the Black-Scholes option-pricing model, uses the following assumptions:

<u>Year Ended December 31,</u>	<u>Expected Term</u>	<u>Expected Volatility Factor</u>	<u>Expected Dividend Amount</u>	<u>Risk-Free Interest Rate</u>
2007	3.0	111.00%	1.93%	4.46%
2008	3.0	87.95%	4.27%	1.77%
2009	3.0	69.56%	2.39%	1.30%

The Company has elected to use the Simplified method for calculating the Expected Term in accordance with SAB 107, and has opted to use the Expected Dividend Amount rather than an Expected Dividend Yield.

The following table summarizes information about the Company's nonvested phantom stock Units at March 31, 2009:

	<u>Units</u>	<u>Weighted Average Grant Date Fair Value</u>
Number of Phantom Stock Unit Awards:		
Nonvested at December 31, 2008	6,892	\$16.24
Granted	8,645	\$14.54
Vested	(2,600)	(\$16.24)
Forfeited	(---)	(\$---)
Canceled	(---)	(\$---)
Nonvested at March 31, 2008	12,937	\$15.64
Phantom Stock Unit Awards Expected to Vest	12,937	\$15.64

At March 31, 2009, a total of 3,508 Units have vested including 2,600, which vested during the first quarter of 2009. The Units granted are expected to vest in one year intervals over three years, subject to earlier termination or forfeiture.

As of March 31, 2009, the unrecognized compensation costs related to Plan Units vesting will be primarily recognized over a period of approximately 3 years.



<u>Fiscal year ending</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>Total</u>
Compensation Expense	\$63	\$68	\$46	\$3	\$180

The Units outstanding and exercisable at March 31, 2009 were in the following exercise price ranges:

<b>Units Outstanding</b>					
<b>Year</b>	<b>Range of Exercise Price</b>	<b>Number of Units Outstanding</b>	<b>Weighted Average Remaining Contractual Life</b>	<b>Weighted Average Exercise Price</b>	<b>Aggregate Intrinsic Value</b>
2007	\$22.02	2,724	0.92	\$22.02	---
2008	\$15.76	5,076	1.92	\$15.76	1
2009	\$15.62	8,645	2.84	\$15.62	4

<b>Units Exercisable</b>					
<b>Year</b>	<b>Range of Exercise Price</b>	<b>Number of Units Exercisable</b>	<b>Weighted-Average Remaining Contractual Life</b>	<b>Weighted-Average Exercise Price</b>	<b>Aggregate Intrinsic Value</b>
2007	\$22.02	---	0.92	\$22.02	---
2008	\$15.76	---	1.92	\$15.76	1
2009	\$15.62	---	2.84	\$15.62	4

## 7. NONCONTROLLING INTERESTS

As of December 31, 2008, the Company's net equity of \$29,384 consisted of \$53 other comprehensive income pertaining to foreign currency translation and \$136 comprehensive income, both related to our Noncontrolling Interest. During the first quarter of 2009 the Noncontrolling Interest represented a \$7 loss and \$3 income within the total Consolidated Company Income of \$385 and Other Comprehensive Loss of \$52, respectively.

**Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations**

*This report contains forward-looking statements, which are subject to inherent uncertainties. These uncertainties include, but are not limited to, variations in weather, changes in the regulatory environment, customer preferences, general economic conditions, increased competition, the outcome of outstanding litigation, and future developments affecting environmental matters. All of these are difficult to predict, and many are beyond the ability of the Company to control.*

*Certain statements in this Quarterly Report on Form 10-Q that are not historical facts, but rather reflect the Company's current expectations concerning future results and events, constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words believes, expects, intends, plans, anticipates, hopes, likely, will, and similar expressions identify such forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or achievements of the Company, or industry results, to differ materially from future results, performance or achievements expressed or implied by such forward-looking statements.*

*Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's view only as of the date of this Form 10-Q. The Company undertakes no obligation to update the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events, conditions or circumstances.*

## OVERVIEW

The Company is a leading manufacturer of flexible metal hose, and is currently engaged in a number of different markets, including construction, manufacturing, transportation, petrochemical, pharmaceutical and other industries.

The Company's business is controlled as a single operating segment that consists of the manufacture and sale of flexible metal hose and accessories. The Company's products are concentrated in residential and commercial construction, and general industrial markets. The Company's primary product line, flexible gas piping, is used for gas piping within residential and commercial buildings. Through its flexibility and ease of use with patented fittings distributed under the trademark AutoFlare®, the TracPipe® and CounterStrike® flexible gas piping systems allows users to substantially cut the time required to install the gas piping, as compared to traditional methods. Most of the Company's products are manufactured at the Company's Exton, Pennsylvania facility with a minor amount of manufacturing performed in the UK. A majority of the Company's sales across all industries are generated through independent outside sales organizations such as sales representatives, wholesalers and distributors, or a combination of both. The Company has a broad distribution network in North America and to a lesser extent in other global markets.

## CHANGES IN FINANCIAL CONDITION

(All dollars in thousands)

During 2009, the Company's inventory balance has decreased \$2,077 from \$10,242 at December 31, 2008 to \$8,165 at March 31, 2009. The decrease is largely due to a focus on inventory management and reductions, along with an inventory write-down resulting from the implementation of updated material standards.

Accrued Compensation has decreased \$1,972 as a result of the annual first quarter scheduled compensation payment less the 2009 accrued expense.

**RESULTS OF OPERATIONS**

(All dollars in thousands)

**Three-months ended March 31, 2009 vs. March 31, 2008**

The Company reported comparative results from continuing operations for the three-month period ended March 31, 2009 and 2008 as follows:

	<b><u>Three-months ended March 31,</u></b> (in thousands)			
	<b><u>2009</u></b> <b><u>(\$000)</u></b>	<b><u>2009</u></b> <b><u>%</u></b>	<b><u>2008</u></b> <b><u>(\$000)</u></b>	<b><u>2008</u></b> <b><u>%</u></b>
Net Sales	\$10,093	100.0%	\$16,423	100.0%
Gross Profit	\$ 4,328	42.9%	\$ 8,180	49.8%
Operating Profits	\$ 622	6.2%	\$ 3,192	19.4%

The Company's sales decreased \$6,330 (38.5%) from \$16,423 in the three-month period ended March 31, 2008 as compared to \$10,093 in the three-month period March 31, 2009.

Revenue for the three-months ended March 31, 2009 reflects the continued decline of the residential construction industry, which was offset some by emerging products and market penetration. Overall volume for the quarter was down 46.5% compared to the prior year quarter.

The Company's gross profit margins decreased from 49.8% in the three-month period ended March 31, 2008 to 42.9% in the three-month period ended March 31, 2009. The decrease in margin is primarily the result of volume related manufacturing burdens and additional reserves for obsolete inventory.

**Selling Expenses.** Selling expenses consist primarily of employee salaries and associated overhead costs, commissions, and the cost of marketing programs such as advertising, trade shows, and related communication costs and freight. Selling expense was \$2,424 and \$1,994 for the three months ended March 31, 2008 and 2009, respectively. The monetary reduction was largely attributable to decreases in commissions and freight related to sales volume. Sales expense as a percentage of sales increased from 15.2% for the three-months ended March 31, 2008 to 19.8% for the three-months ended March 31, 2009, largely due to the fixed selling costs in relation to the sales reduction, but also related to an increase in advertising related activities.

**General and Administrative Expenses.** General and administrative expenses consist primarily of employee salaries, benefits for administrative, executive, and finance personnel, legal and accounting, and corporate general and administrative services. General and administrative expenses were \$1,891 and \$1,163 for the three months ended March 31, 2008 and 2009, respectively. The \$728 decrease in expenses is partially attributable to the cash settlement of the Parker Hannifin case, as outlined in the Company's December 31, 2008 Form 10-K, which





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resulted in income of \$265. There was also a decrease in staffing related expenses and consulting fees. Administrative expense, as a percentage of sales, was flat at 11.5% for the three months ended March 31, 2008 and March 31, 2009.

**Engineering Expense.** Engineering expenses consist of development expenses associated with the development of new products and enhancements to existing products, and manufacturing engineering costs. Engineering expenses were \$603 and \$549 for the three months ended March 31, 2008 and 2009, respectively. Engineering expenses as a percentage of sales increased from 3.7% for the three months ended March 31, 2008 to 5.4% for the three months ended March 31, 2009.

Reflecting all of the factors mentioned above, Operating Profit margins decreased \$2,570 from a profit of \$3,192 in the three-month period ended March 31, 2008 to a profit of \$622 in the three-month period ended March 31, 2009.

**Interest Income (Expense)-Net.** Interest income-net includes interest income on the note receivable from Mestek for the first quarter of 2008, and interest income on our interest-bearing investments for both quarters ending March 31, 2008 and 2009.

**Other Income-Net.** Other Income-net primarily consists of foreign currency exchange gains (losses) on transactions with Omega Flex Limited, our U.K. subsidiary.

**Income Tax Expense.** The Company's effective tax rate in 2009 approximates the 2008 rate and does not differ materially from expected statutory rates.

### **CRITICAL ACCOUNTING POLICIES AND USE OF ESTIMATES**

**(All dollars are in thousands)**

Financial Reporting Release No. 60, released by the Securities and Exchange Commission, requires all companies to include a discussion of critical accounting policies or methods used in the preparation of financial statements. Note 2 of the Notes to the Consolidated Financial Statements include a summary of the significant accounting policies and methods used in the preparation of our Consolidated Financial Statements. The following is a brief discussion of the Company's more significant accounting policies.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The most significant estimates and assumptions relate to revenue recognition, accounts receivable valuations, inventory valuations, goodwill and intangible asset valuations, product liability costs, workers compensation claims reserves, health care claims reserves, and accounting for income taxes. Actual amounts could differ significantly from these estimates.



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Our critical accounting policies and significant estimates and assumptions are described in more detail as follows:

### **Revenue Recognition**

The Company's revenue recognition activities relate almost entirely to the manufacture and sale of flexible metal hose and pipe. Under generally accepted accounting principles, revenues are considered to have been earned when the Company has substantially accomplished what it must do to be entitled to the benefits represented by the revenues. The following criteria represent preconditions to the recognition of revenue:

Persuasive evidence of an arrangement for the sale of product or services must exist.

Delivery has occurred or services rendered.

The sales price to the customer is fixed or determinable.

Collection is reasonably assured.

The Company generally recognizes revenue upon shipment in accordance with the above principles.

Gross sales are reduced for all consideration paid to customers for which no identifiable benefit is received by the Company. This includes promotional incentives, year-end rebates, and discounts. The amounts of certain incentives are estimated at the time of sale.

Commissions, for which the Company receives an identifiable benefit, are accounted for as a sales expense.

### **Accounts Receivable**

Accounts receivable are reduced by an allowance for amounts that may become uncollectible in the future. The estimated allowance for uncollectible amounts is based primarily on specific analysis of accounts in the receivable portfolio and historical write-off experience. While management believes the allowance to be adequate, if the financial condition of the Company's customers were to deteriorate, resulting in impairment of their ability to make payments, additional allowances may be required.

### **Inventory**

Inventories are valued at the lower of cost or market. Cost of inventories are determined by the first-in, first-out (FIFO) method. The Company generally considers inventory quantities beyond two-years usage, measured on a historical usage basis, to be excess inventory and reduces the

gross carrying value of inventory accordingly.

**Goodwill and Intangible Assets**

In accordance with FAS 142, the Company ceased recording amortization of goodwill and intangible assets with indefinite lives effective January 1, 2002. The Company performed annual impairment tests in accordance with FAS 142, where fair value of the reporting unit was

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compared to the carrying amount. The fair value of the reporting unit exceeded the carrying amounts, therefore as of December 31, 2008 the analysis showed no impairment of goodwill.

### **Product Liability Reserves**

As explained more fully under Contingencies, the Company retains liability for the first \$50 of product liability claims. To date, the Company has not experienced a meaningful product failure rate.

### **Workers Compensation Claims Reserves**

The Company is insured on a first dollar basis for workers compensation.

### **Health Care Claim Reserves**

The Company's liability is limited to \$35 per case and an aggregate of \$660 annually.

### **Accounting for Income Taxes**

The Company accounts for federal tax liabilities in accordance with SFAS No. 109, Accounting for Income Taxes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. 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 effect on deferred tax assets and liabilities from a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided for deferred tax assets if it is more likely than not that these items will either expire before the Company is able to realize the benefit, or that future deductibility is uncertain.

## **LIQUIDITY AND CAPITAL RESOURCES**

(All amounts in thousands except share amounts)

### **Three Months ended March 31, 2009**

As of March 31, 2009, we had \$8,917 in consolidated cash and cash equivalents, which is \$856 less than at December 31, 2008.

**Operating Activities**

Cash used in operations for the first three months of 2009 was \$491 compared with \$1,697 used in the first three months of 2008, a \$1,206 decrease.

**Investing Activities**

Capital spending was \$313 and \$102 in the first quarters ended March 31, 2009 and March 31, 2008, respectively.

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## **Financing**

Cash used in financing activities during the first three months of 2009 was \$24 compared with \$7,432 used in the first three months of 2008. The most significant component for the first three months of 2008 was the \$7,092 related to the special dividend.

On September 12, 2007, the Company announced that its Board of Directors has authorized the purchase of up to \$5,000 of its common stock. The purchases may be made from time-to-time in open market or in privately negotiated transactions, depending on market and business conditions, within the next 24 months. The Board retained the right to cancel, extend, or expand the share buyback program at any time and from time-to-time. During the first quarter of 2009, the Company had purchased 1,986 shares of treasury stock for \$24.

On September 18, 2008, the Company extended its Revolving Line of Credit Note and a Loan Agreement with Sovereign Bank, N.A., whereby the company established a line of credit facility for a one-year duration ending September 4, 2009, and in the maximum amount of \$7,500. The loan agreement provides for the payment of any loan under the agreement at a rate that is either prime rate less 1%, or LIBOR rate plus 1%. Under the terms of the agreement, the Company is required to pay a nominal commitment fee, and is also delegated to pay a Line Fee equal to one-tenth percent (0.10%) of the average unused balance on a quarterly basis. As of March 31, 2009, the Company does not have any loans or loan balances outstanding under the loan agreement.

The Company believes its liquidity position as of March 31, 2009 is fully adequate to meet foreseeable future needs and that the Company will possess adequate cash reserves to meet its day-to-day needs including any acquisitions or capital expenditures or stock repurchases it can reasonably foresee at this time.

## **CONTINGENT LIABILITIES AND GUARANTEES**

See Note 5 to the Company's financial statements.

## **OFF-BALANCE SHEET ARRANGEMENTS**

Refer to Item 7 of the Company's 2008 year-end Form 10-K under the caption "Tabular Disclosure of Contractual Obligations and Off-Balance Sheet Arrangements".



**Item 3. Quantitative And Qualitative Information About Market Risks**

The Company does not engage in the purchase or trading of market risk sensitive instruments. The Company does not presently have any positions with respect to hedge transactions such as forward contracts relating to currency fluctuations. No market risk sensitive instruments are held for speculative or trading purposes.

**Item 4 Controls And Procedures**

- (a) Evaluation of Disclosure Controls and Procedures.

At the end of the fiscal first quarter of 2009, the Company evaluated the effectiveness of the design and operation of its disclosure controls and procedures. The Company's disclosure controls and procedures are designed to ensure that the Company records, processes, summarizes and reports in a timely manner the information required to be disclosed in the periodic reports filed by the Company with the Securities and Exchange Commission. The Company's management, including the chief executive officer, chief financial officer and principal accounting officer, have conducted an evaluation of the effectiveness of the design and operation of the Company's Disclosure Controls and Procedures as defined in the Rule 13a-15(e) of Securities Exchange Act of 1934. Based on that evaluation, the chief executive officer, chief financial officer and principal accounting officer have concluded that, as of the date of this report, the Company's disclosure controls and procedures are effective to provide reasonable assurance of achieving the purposes described in Rule 13a-15(e), and no changes are required at this time.

- (b) Changes in Internal Controls.

There was no change in the Company's internal control over financial reporting (as defined in rule 13a-15(f) of the Securities Exchange Act of 1934) identified in connection with the evaluation required by Rule 13a-15(d) of the Securities Exchange Act of 1934 that occurred during the three-month period covered by this Report on Form 10-Q that has materially affected or is reasonably likely to materially affect the Company's internal control over financial reporting subsequent to the date the chief executive officer and chief financial officer and principal accounting officer completed their evaluation.

**PART II - OTHER INFORMATION**

**Item 1 Legal Proceedings**

See Note 5 Contingencies of the Notes to the Condensed Consolidated Financial Statements (Part 1, Item 1) for information regarding legal proceedings in which we are involved.

**Item 4 Submission of Matter to a Vote of the Security Holders**

No matters were submitted to the security holders of the Company for a vote during the first quarter of 2009.



**Item 6 - Exhibits**

**Exhibit**

<b><u>No.</u></b>	<b><u>Description</u></b>
31.1	Certification of Chief Executive Officer of Omega Flex, Inc. pursuant to Rule 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
31.2	Certification of Chief Financial Officer of Omega Flex, Inc. pursuant to 15d-14(a) promulgated under the Securities Exchange Act of 1934, as amended.
32.1	Certification of Chief Executive Officer and Chief Financial Officer of Omega Flex, Inc., pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**SIGNATURES**

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

OMEGA FLEX, INC.  
(Registrant)

Date: May 8, 2009

By: /S/ Paul J. Kane  
Paul J. Kane  
Vice President Finance  
and Chief Financial Officer