

Omega Flex, Inc.  
Form 10-Q  
May 14, 2008  
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, 2008**

**( ) 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, 2008 was 10,106,408.

OMEGA FLEX, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR THE THREE MONTHS ENDED MARCH 31, 2008

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

	<b>March 31, <u>2008</u> (unaudited) (Dollars in thousands)</b>	<b>December 31 <u>2007</u></b>
<b>ASSETS</b>		
Current Assets		
Cash and Cash Equivalents	\$ 3,924	\$13,143
Accounts Receivable - less allowances of \$137 and \$137, respectively	9,515	10,132
Inventories	10,347	10,567
Note Receivable from former Parent Company	3,250	3,250
Other Current Assets	<u>1,779</u>	<u>1,884</u>
Total Current Assets	<u>28,815</u>	<u>38,976</u>
Property and Equipment - net	6,705	6,749
Goodwill	3,526	3,526
Other Long Term Assets	<u>520</u>	<u>521</u>
Total Assets	\$39,566 =====	\$49,772 =====
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts Payable	\$1,287	\$1,486
Accrued Compensation	871	2,692
Accrued Commissions & Sales Incentives	1,884	3,032
Accrued Legal Settlement and Related Costs	253	1,272
Dividends Payable	---	7,092
Other Liabilities	<u>2,761</u>	<u>2,423</u>
Total Current Liabilities	7,056	17,997
Long-Term portion of Accrued Legal Settlement	---	1,000
Other Long-Term Liabilities	<u>2,114</u>	<u>2,107</u>
Total Liabilities	<u>9,170</u>	<u>21,104</u>
Minority Interests	<u>142</u>	<u>129</u>
Shareholders' Equity:		
Common Stock par value \$0.01 Share: authorized 20,000,000 Shares: 10,106,408 and 10,128,516 shares issued and outstanding at		
March 31, 2008 and December 31, 2007, respectively	102	102
Paid in Capital	11,032	11,372
Retained Earnings	18,721	16,651
Accumulated Other Comprehensive Income	<u>399</u>	<u>414</u>
Total Shareholders' Equity	<u>30,254</u>	<u>28,539</u>

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Total Liabilities and Shareholders' Equity	\$39,566	\$49,772
	=====	=====
See Accompanying Notes to Consolidated Financial Statements.		

## OMEGA FLEX, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

	<b>For the three-months ended March 31,</b>	
	<b><u>2008</u></b>	<b><u>2007</u></b>
	<b>(Amounts in thousands, except earnings per Common Share)</b>	
Net Sales	\$16,423	\$17,331
Cost of Goods Sold	<u>8,243</u>	<u>9,055</u>
Gross Profit	8,180	8,276
Selling Expense	2,494	2,827
General and Administrative Expense	1,997	1,863
Legal Settlement and Related Costs	(106)	164
Engineering Expense	<u>603</u>	<u>606</u>
Operating Profit	3,192	2,816
Interest Income, Net	102	189
Other Income, Net	<u>12</u>	<u>1</u>
Income Before Income Taxes	3,306	3,006
Income Tax Expense	<u>1,237</u>	<u>1,134</u>
Net Income	\$2,069 =====	\$1,872 =====
Basic Earnings per Common Share:		
Net Income	\$0.21	\$0.18
Basic Weighted Average Shares Outstanding	10,113	10,154
Diluted Earnings per Common Share:		
Net Income	\$0.21	\$0.18
Diluted Weighted Average Shares Outstanding	10,113	10,154

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>2008</u></b>	<b><u>2007</u></b>
	<b>(Dollars in thousands)</b>	
Cash Flows from Operating Activities:		
Net Income	\$2,069	\$1,872
Adjustments to Reconcile Net Income to		
Net Cash Provided by Operating Activities:		
Depreciation and Amortization	146	96
Non-Cash Compensation Expense	15	10
Provision for Losses on Accounts Receivable, net of write-offs and recoveries	---	21
Change in Minority Interests	13	6
Changes in Assets and Liabilities:		
Accounts Receivable	617	825
Inventory	220	(2,084)
Accounts Payable	(199)	1,525
Accrued Compensation	(1,821)	(1,633)
Accrued Legal Settlement and Related Costs	(2,019)	(5,983)
Other Liabilities	(844)	(3,320)
Other Assets	<u>106</u>	<u>148</u>
Net Cash (Used In) Operating Activities	<u>(1,697)</u>	<u>(8,518)</u>
Cash Flows from Investing Activities:		
Capital Expenditures	<u>(102)</u>	<u>(68)</u>
Net Cash Used in Investing Activities	<u>(102)</u>	<u>(68)</u>
Cash Flows from Financing Activities:		
Treasury Stock Purchase	(340)	---
Dividends Paid	<u>(7,092)</u>	<u>(4,061)</u>
Net Cash Used in Financing Activities	<u>(7,432)</u>	<u>(4,061)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(9,231)	(12,647)
Translation effect on cash	(12)	(3)
Cash and Cash Equivalents    Beginning of Period	<u>13,143</u>	<u>17,424</u>
Cash and Cash Equivalents    End of Period	<u>\$3,924</u>	<u>\$4,774</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, 2008 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, and sells its product through distributors, wholesalers and to original equipment manufacturers (OEMs) throughout North America, and in certain European markets.

### 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.

**Stock Based Compensation**

Effective January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards ( SFAS ) No. 123 (Revised 2004), *Share-Based Payment*. Under the provisions of Statement of Financial Accounting Standards ( SFAS ) No. 123 (Revised 2004), *Share-Based Payment* SFAS 123R, the Company recognizes the estimated fair value of stock based compensation in the consolidated statement of operations over the requisite service period of each option granted. Under the modified prospective application method of SFAS 123R, the Company applies the provisions of SFAS 123R to all awards granted or modified after January 1, 2006, as well as any unvested awards outstanding on January 1, 2006. The Company had no stock options outstanding at December 31, 2007 and made no option grants during 2007 or 2008.

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During 2006, the Company established the Omega Flex, Inc. 2006 Phantom Stock Plan as described in detail in Note 7 under the caption "Stock Based Plans". In accordance with SFAS 123R, the Company recorded compensation expense of approximately \$7 in 2008 related to the Phantom Stock Plan.

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**Currency Translation**

Assets and liabilities denominated in foreign currencies are translated into U.S. dollars at 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. Under this method the Company recorded tax expense and related deferred taxes and tax benefits.

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, 2008 and 2007, respectively, the components of Other Comprehensive (Loss) Income consisted solely of foreign currency translation adjustments.

**New Accounting Pronouncements**

Effective January 1, 2008, the Company prospectively implemented the provisions of Statement of Financial Accounting Standard ( SFAS ) No. 157, Fair Value Measurements for financial assets and financial liabilities reported or disclosed at fair value. At March 31, 2008, there were no applicable financial assets or financial liabilities that required fair value measurements. Accordingly, the impact of adopting these SFAS 157 provisions on the Company's financial statements had no material effect on the Company's financial position, results of operations, or liquidity.

In February 2008, the Financial Accounting Standards Board ( FASB ) issued FASB Staff Position ( FSP ) No. 157-2, which delayed until the first quarter of 2009 the effective date of SFAS 157 provisions concerning non-financial assets and non-financial liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis. Also in February 2008, the FASB issued FSP No. 157-1 to exclude SFAS No. 13, Accounting for Leases, and its related interpretative accounting pronouncements from the scope of SFAS 157. The Company continues to evaluate the impact of these provisions, but does not anticipate that they will have a material effect on the Company's financial position, results of operations, or liquidity.

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The Company also adopted, effective January 1, 2008, the provisions of SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities," including an amendment of SFAS No. 115. SFAS 159 provided an option to the Company to measure eligible assets and liabilities at fair value with changes in value recognized in earnings. Fair value recognition may be elected either upon initial recognition of an eligible asset or liability or, for an existing asset or liability, if an event triggers a new basis of accounting. The Company did not elect to remeasure any existing financial assets or liabilities under the provisions of SFAS 159. Accordingly, the impact of adopting these SFAS 159 provisions on the Company's financial statements had no material effect on the Company's financial position, results of operations, or liquidity.

In December 2007, the Financial Accounting Standards Board (FASB) issued SFAS No. 160 "Non-controlling Interests in Consolidated Financial Statements" an amendment of ARB No. 51 (SFAS 160). SFAS 160 establishes accounting and reporting standards for the non-controlling interest in a subsidiary and for the deconsolidation of a subsidiary. The guidance applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. An entity may not apply it before that date. The Company believes that this new pronouncement will not have any significant impact on the Company's financial statements in future periods.

In December 2007, the FASB issued SFAS No. 141 (R) "Business Combinations" (SFAS 141R). SFAS 141R establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree. SFAS 141R also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. The guidance applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. An entity may not apply it before that date. The Company believes that this new pronouncement will have an impact on our accounting for future business combinations once adopted, but the effect is dependent upon the acquisitions that are made in the future.

In March 2008, FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities" an amendment of FASB Statement No. 133 which establishes the disclosure requirements for derivative instruments and for hedging activities. This Statement amends and expands the disclosure requirements of Statement 133 with the intent to provide users of financial statements with an enhanced understanding of derivative instruments and hedging activities. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early adoption encouraged. We do not expect adoption of SFAS 161 to have a material impact on the Company's financial statements.

### **Reclassifications**

Certain reclassifications have been made to prior years' financial statements to conform to the 2008 presentation.

### 3. DISTRIBUTION FROM MESTEK, INC. (Spin-Off)

The Company completed a Spin-Off from its former parent, Mestek, Inc. (Mestek) on July 29, 2005. The Company's common shares began trading on the NASDAQ Global Market under the trading symbol OFLX on August 1, 2005.

In connection with the Spin-Off, the Company executed certain agreements governing its relationship with Mestek subsequent to the date of the Spin-Off which are disclosed in the initial Form 10 and also discussed in detail in Note 3 of the December 31, 2006 Form 10-K filing.

At the effective date of the Spin-Off, Mestek was indebted to the Company in the amount of \$3,250 which was converted on the effective date of the Spin-Off to a 3-year note receivable from Mestek bearing interest at 100 basis points above the then prevailing 3-year US Treasury note yield at approximately 5%. The principal balance of the Note at March 31, 2008 and December 31, 2007 remained \$3,250. The interest income recorded on the note was approximately \$41 for the three months ended 2008 and 2007, respectively.

In connection with the Mestek Note, on October 19, 2007 the Company entered into a Subordination Agreement with Bank of America, N.A. Under the Agreement, Mestek shall be permitted to repay any regularly scheduled payment of the subordinated debt to the Company provided that, at the time of repayment there exists no event of default under the terms of Mestek's loan agreement with Bank of America, or an instance of insolvency or bankruptcy. If Mestek were to default under its loan agreement with Bank of America, or if it became insolvent, then the Company's rights to collect the amounts due under the Mestek Note would become subordinate to the rights of Bank of America under its loan agreement with Mestek.

### 4. INVENTORIES

Inventories consisted of the following at March 31:

	<u>2008</u> (unaudited) (dollars in thousands)	<u>2007</u>
Finished Goods	\$7,652	\$7,150
Raw Materials	<u>2,695</u>	<u>3,417</u>
Total Inventory	\$10,347 =====	\$10,567 =====

### 5. SHAREHOLDERS' EQUITY

(Amounts in thousands, except share amounts)

As of March 31, 2008 and December 31, 2007, the Company had authorized 20,000,000 common stock shares with par value of \$0.01 per share, and had 10,106,408 and 10,128,516 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.

Our future decisions concerning the payment of dividends on our common stock will depend upon our results of operations, financial condition and capital expenditure plans, as well as such other factors as the Board of Directors, in its sole discretion, may consider relevant.

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 2008, the Company purchased 22,108 shares for \$340. Since inception, the Company has purchased in total 47,225 shares for approximately \$700.

### 6. COMMITMENTS AND CONTINGENCIES

#### Commitments:

On September 5, 2006 the Company and other defendants entered into a Stipulation and Settlement Agreement with the Class Representatives and Class Counsel, to settle and resolve the allegations brought forth in the lawsuit titled *Lovelis, et al. v. Titeflex Corp., Inc., et al.* in the Arkansas Circuit Court, Clark County. Both the Company and the other defendants denied these allegations, and denied any wrongdoing or legal liability, but agreed to settle this matter to avoid further cost and the uncertainty and risk of the outcome of further litigation. Under the Settlement Agreement, the Company agreed to pay the value of each payment voucher redeemed by a class member for the installation of a lightning protection system or bonding and grounding of the Company's CSST product. The amount of the voucher is dependent on the geographical area in the United States where the building is located and the size of the heated or air-conditioned area of the building. The Company also agreed to pay a fixed amount of administrative expenses and attorneys' fees to the Class Counsel.

The Company cannot determine the exact amount for which it may be liable for the costs of the payment vouchers tendered under the claim program, because of the number of unknown variables associated with this liability. However, the Company estimated that the total amount of the liability relating to the settlement of the litigation would fall within a range of approximately \$8,810 and \$10,200. Thus far the Company has paid approximately \$8,421 related to the Settlement with a remaining liability of \$239 Short-Term Liability. This amount is based on currently available information and certain estimates and judgments, and is subject to revision as actual claims are received. In addition, there is a \$14 current liability for legal services related to the Settlement. As of March 31, 2008, the third party administrator of the settlement program has received 775 claims relating to the Company's products in connection with the Settlement.

Included in the payments noted above, and as indicated in Note 15 of the Company's December 31, 2007 Form 10-K, on February 4, 2008, the Company reached an agreement for final payment relating to the class action settlement, excluding the outstanding vouchers. This

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final payment, which was made on March 3, 2008, in the amount of \$1,850, represents the \$1,000 current portion due as previously disclosed, and the remaining \$1,000 long-term portion which was due in March of 2009, less a \$150 (15%) reduction resulting from early payment.

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 \$312 for March 31, 2008 and December 31, 2007, 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 \$521 at March 31, 2008 and December 31, 2007, 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.

The Company's liability is limited to \$30 per case and an aggregate of \$620 annually for health insurance.

### **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.

## 7. 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. 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 have 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 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, 2007, the Company had 2,724 units outstanding, all of which were granted at *Full Value*. On March 6, 2008, the Company granted an additional 5,076 *Full Value* Units with a face value of \$80 (fair value at grant date of approximately \$70). In all cases, the grant price was equal to the closing price of the Company's common stock at the grant date.

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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 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, 2008.

The fair value of the Units granted through the first quarter March 31, 2008 using the Black-Scholes option-pricing model, uses the following assumptions:

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

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.

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The following table summarizes information about phantom stock the Units outstanding at March 31, 2008:

	<u>Units</u>	<u>Weighted Average Grant Date Fair Value</u>
Number of Phantom Stock Unit Awards:		
Outstanding at December 31, 2007	2,724	\$20.38
Granted	5,076	\$13.86
Vested	(---)	(\$---)
Forfeited	(---)	(\$---)
Canceled	(---)	(\$---)
Outstanding at March 31, 2008	7,800	\$16.74
Phantom Stock Unit Awards Expected to Vest	7,800	\$16.74

At March 31, 2008 none of the Units have vested. The Units granted are expected to vest in three year intervals, subject to earlier termination or forfeiture.

As of March 31, 2008, 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>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Total</u>
Compensation Expense	\$38	\$42	\$26	\$4	\$110

The Units outstanding and exercisable at March 31, 2008 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	1.92	\$22.02	---
2008	\$15.76	5,076	2.92	\$15.76	5

<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	---	1.92	\$22.02	---
2008	\$15.76	---	2.92	\$15.76	5



**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 2008, the Company's cash balance has decreased \$9,219 from \$13,143 at December 31, 2007 to \$3,924 at March 31, 2008. Some of the major transactions that affected our cash balance were a \$7,092 special dividend payment made on January 16, 2008, and a payment of \$1,850 on March 3, 2008 to the Settlement Agreement as outlined in Note 15 of the year-end Form 10-K. Those payments were partially offset by cash generated from earnings for the year.

As discussed in Note 5, Shareholders' Equity, in December of 2007 the Company declared a dividend, which amounted to \$7,092. The Company subsequently paid the dividend on January 16, 2008.

**RESULTS OF OPERATIONS**

(All dollars in thousands)

**Three-months ended March 31, 2008 vs. March 31, 2007**

The Company reported comparative results from continuing operations for the three-month period ended March 31, 2008 and 2007 as follows:

	<b><u>Three-months ended March 31,</u></b> (in thousands)			
	<b><u>2008</u></b> <b><u>(\$000)</u></b>	<b><u>2008</u></b> <b><u>%</u></b>	<b><u>2007</u></b> <b><u>(\$000)</u></b>	<b><u>2007</u></b> <b><u>%</u></b>
Net Sales	\$16,423	100.0%	\$17,331	100.0%
Gross Profit	\$ 8,180	49.8%	\$ 8,276	47.8%
Operating Profits	\$ 3,192	19.4%	\$ 2,816	16.2%

The Company's sales decreased \$908 (5.2%) from \$17,331 in the three-month period ended March 31, 2007 as compared to \$16,423 in the three-month period March 31, 2008.

Revenue for the three-months ended March 31, 2008 reflects continued weakness in the residential construction industry, which was offset somewhat by gains in market share in residential, non-residential and international construction markets. Overall volume for the quarter was down 18.1% compared to the prior year quarter.

The Company's gross profit margins increased from 47.8% in the three-month period ended March 31, 2007 to 49.8% in the three-month period ended March 31, 2008. The increase in margin is primarily the result of a decrease in the cost of the Company's primary raw materials during the quarter; in particular stainless steel combined with strategic price increases implemented in the last half of 2007, and other manufacturing efficiencies.

**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 \$2,827 and \$2,494 for the three months ended March 31, 2007 and 2008, respectively. The reduction was largely attributable to decreases in commissions and freight related to sales volume. Sales expense as a percentage of sales decreased from 16.3% for the three-months ended March 31, 2007 to 15.2% for the three-months ended March 31, 2008.

**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 \$1,863 and \$1,997 for the three months ended March 31, 2007 and 2008, respectively. The \$134 increase in expenses is mostly attributable to an increase in staffing related expenses, and consulting fees. For the preceding reasons, general and



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administrative expense, as a percentage of sales, increased from 10.7% for the three months ended March 31, 2007 to 12.2% for the three months ended March 31, 2008.

Legal Settlement and Related Costs. Legal charges related to the Arkansas litigation in the three months of 2007 and 2008, were \$164 and (\$106), respectively. The Company recognized a \$150 reduction in legal costs in 2008 due to the early class action settlement payment in March of 2008 as disclosed in Note 6, Commitments and Contingencies. The majority of the costs associated with this litigation are behind the Company.

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 \$606 and \$603 for the three months ended March 31, 2007 and 2008 respectively. Accordingly, engineering expenses as a percentage of sales were in line with the prior year at 3.5% for the three months ended March 31, 2007 and 3.7% for the three months ended March 31, 2008.

Reflecting all of the factors mentioned above, Operating Profit margins increased \$376 from a profit of \$2,816 in the three-month period ended March 31, 2007 to a profit of \$3,192 in the three-month period ended March 31, 2008.

Interest Income-Net. Interest income-net includes interest income on the note receivable from Mestek and interest income on our interest-bearing investments.

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 2008 approximates the 2007 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.



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**

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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.

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**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 its annual impairment test in accordance with FAS 142 as of December 31, 2007 which indicated 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 \$30 per case and an aggregate of \$620 annually.

**Accounting for Income Taxes**

The Company accounts for federal tax liabilities in accordance with SFAS No. 109, Accounting for Income Taxes. Under this method the Company recorded tax expense and related deferred taxes and tax benefits.

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, 2008**

As of March 31, 2008, we had \$3,924 in consolidated cash, cash equivalents and short-term investments, which is \$9,219 less than at December 31, 2007, mostly resulting from cash payments of \$7,092 for a special dividend, and \$1,850 related to the Legal Settlement discussed in Note 6. The decrease was partially offset by cash generated from earnings for the year.

**Operating Activities**

Cash used in operations for the first three months of 2008 was \$1,697 compared with \$8,514 used in the first three months of 2007, a \$6,817 decrease. The most significant component was the \$1,850 and \$6,000 payments related to the Legal Settlement made in the first three months of 2008 and 2007, respectively.

**Investing Activities**

Capital spending was \$102 and \$68 in the first quarters ended March 31, 2008 and March 31, 2007, respectively.

**Financing**

Cash used in financing activities during the first three months of 2008 was \$7,432 compared with \$4,061 used in the first three months of 2007. 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 2008, the Company had purchased 22,108 shares of treasury stock for \$340.

The Company entered into a 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, 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%. As of March 31, 2008 the Company does not have any loans or loan balances, under the loan agreement.

The Company believes its liquidity position as of March 31, 2008 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 6 to the Company's financial statements.

**OFF-BALANCE SHEET ARRANGEMENTS**

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Refer to Item 7 of the Company's 2007 year-end Form 10-K under the caption "Tabular Disclosure of Contractual Obligations and Off-Balance Sheet Arrangements".

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**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 2008, 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**

On September 4, 2006, the Company entered into the Stipulation and Settlement Agreement between the Class Representatives and Class Counsel and the Company and all of the other defendants in the lawsuit titled Lovelis, et al. v. Titeflex, Inc., et al. The Settlement Agreement was filed on September 5, 2006 in the Arkansas Circuit Court in Clark County, preliminarily settling all of the allegations set forth in the lawsuit. On September 6, 2006, the Company issued a press release and filed a Current Report on Form 8-K with the Securities and Exchange Commission regarding the settlement. On February 1, 2007, the Circuit Court gave

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final approval of the Settlement Agreement and dismissed the case. The remedial program provided under the Settlement Agreement, processed claims from class members during the claim period. The deadline for submitting any claims was September 5, 2007.

See Note 6 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 2008.

### **Item 5 Material Definitive Agreement with Executive Officer**

The Company has entered into a consulting agreement with E. Lynn Wilkinson, the Company's Vice President Finance and Chief Financial Officer. Mr. Wilkinson has previously announced his retirement, and the agreement becomes effective upon his retirement, May 19, 2008. Mr. Wilkinson will provide limited and part-time management services relating to the finance and accounting, assist in the preparation of financial statements, and perform other services as requested. The agreement is for a term of six months, and may be renewed for successive 90-day periods by the mutual consent of the parties. The Company will pay to Mr. Wilkinson a retainer of \$52,000, which is equal to one-half of his regular base pay at the time of his retirement for the six-month period. Mr. Wilkinson will not receive any other compensation or benefits under the agreement.

**Item 6 - Exhibits**

**Exhibit**

<b><u>No.</u></b>	<b><u>Description</u></b>
10.1	Material Definitive Agreement with an Executive Officer of the Company, effective May 19, 2008.
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.
31.3	Certification of Principal Accounting 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, Chief Financial Officer and Principal Accounting 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 14, 2008

By: /S/ E. Lynn Wilkinson  
E. Lynn Wilkinson  
Vice President Finance  
and Chief Financial Officer