HALF ROBERT INTERNATIONAL INC /DE/
Form 10-Q
August 02, 2010

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 JUNE 30, 2010

OR

¨ **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 1-10427

ROBERT HALF INTERNATIONAL INC.

(Exact name of registrant as specified in its charter)

Delaware	**94-1648752**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
2884 Sand Hill Road	
Suite 200	
Menlo Park, California	**94025**
(Address of principal executive offices)	**(zip-code)**

Registrant s telephone number, including area code: (650) 234-6000

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. (Check one):

Large accelerated filer	x	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 x

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of June 30, 2010:

147,590,437 shares of $.001 par value Common Stock

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ROBERT HALF INTERNATIONAL INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

(in thousands, except share amounts)

	June 30, 2010	December 31, 2009
ASSETS		
Cash and cash equivalents	$ 290,044	$ 365,794
Accounts receivable, less allowances of $19,405 and $21,423	384,642	362,392
Current deferred income taxes	94,158	51,643
Other current assets	128,779	142,805
Total current assets	897,623	922,634
Goodwill	188,613	189,336
Other intangible assets, net	77	392
Property and equipment, net	108,318	124,658
Deferred and other income taxes	19,639	46,515
Total assets	$ 1,214,270	$ 1,283,535
LIABILITIES		
Accounts payable and accrued expenses	$ 96,629	$ 101,610
Accrued payroll costs and retirement obligations	259,315	265,245
Income taxes payable	1,597	
Current portion of notes payable and other indebtedness	118	113
Total current liabilities	357,659	366,968
Notes payable and other indebtedness, less current portion	1,719	1,779
Other liabilities	26,071	14,978
Total liabilities	385,449	383,725
Commitments and Contingencies (Note G)		
STOCKHOLDERS EQUITY		
Preferred stock, $.001 par value authorized 5,000,000 shares; issued and outstanding zero shares		
Common stock, $.001 par value authorized 260,000,000 shares; issued and outstanding 147,575,541 shares and 148,645,335 shares	148	149
Capital surplus	797,769	854,081
Accumulated other comprehensive income	30,904	45,580
Retained earnings		
Total stockholders equity	828,821	899,810
Total liabilities and stockholders equity	$ 1,214,270	$ 1,283,535

The accompanying Notes to Condensed Consolidated Financial Statements are

an integral part of these financial statements.

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ROBERT HALF INTERNATIONAL INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

(in thousands, except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2010	2009	2010	2009
Net service revenues	$ 769,090	$ 749,887	$ 1,506,263	$ 1,573,212
Direct costs of services, consisting of payroll, payroll taxes, insurance costs and reimbursable expenses	479,232	484,830	948,277	1,014,427
Gross margin	289,858	265,057	557,986	558,785
Selling, general and administrative expenses	267,519	255,007	523,187	532,057
Amortization of intangible assets	46	280	315	898
Interest income, net	(94)	(455)	(168)	(1,075)
Income before income taxes	22,387	10,225	34,652	26,905
Provision for income taxes	10,206	4,809	13,996	12,701
Net income	$ 12,181	$ 5,416	$ 20,656	$ 14,204
Net income available to common stockholders	$ 11,660	$ 4,801	$ 19,286	$ 13,110
Net income per share (Note J):				
Basic	$ .08	$ .03	$ .13	$ .09
Diluted	$ .08	$ .03	$ .13	$ .09
Shares:				
Basic	143,100	146,443	143,667	146,660
Diluted	144,331	147,044	144,999	147,092
Cash dividends declared per share	$ .13	$ .12	$ .26	$ .24

The accompanying Notes to Condensed Consolidated Financial Statements are

an integral part of these financial statements.

ROBERT HALF INTERNATIONAL INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY (UNAUDITED)

(in thousands, except per share amounts)

	Six Months Ended June 30,	
	2010	**2009**
COMMON STOCK SHARES:		
Balance at beginning of period	148,645	150,943
Net issuances of restricted stock	1,410	2,310
Repurchases of common stock	(2,726)	(2,696)
Exercises of stock options	247	1,264
Balance at end of period	147,576	151,821
COMMON STOCK PAR VALUE:		
Balance at beginning of period	$ 149	$ 151
Net issuances of restricted stock	1	2
Repurchases of common stock	(2)	(2)
Exercise of stock options		1
Balance at end of period	$ 148	$ 152
CAPITAL SURPLUS:		
Balance at beginning of period	$ 854,081	$ 949,474
Net issuances, and other changes to, restricted stock excess over par value	(1)	(2)
Repurchases of common stock excess over par value	(55,674)	(43,465)
Cash dividends ($.26 per share and $.24 per share)	(34,114)	(36,438)
Stock-based compensation expense	29,124	30,686
Exercises of stock options excess over par value	5,385	17,906
Tax impact of equity incentive plans	(1,032)	1,196
Balance at end of period	$ 797,769	$ 919,357
ACCUMULATED OTHER COMPREHENSIVE INCOME:		
Balance at beginning of period	$ 45,580	$ 34,263
Translation adjustments	(14,676)	7,397
Balance at end of period	$ 30,904	$ 41,660
RETAINED EARNINGS:		
Balance at beginning of period	$	$
Repurchases of common stock excess over par value	(16,085)	(14,204)
Cash dividends ($.26 per share)	(4,571)	
Net income	20,656	14,204
Balance at end of period	$	$

The accompanying Notes to Condensed Consolidated Financial Statements are

an integral part of these financial statements.

ROBERT HALF INTERNATIONAL INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(in thousands)

	Six Months Ended June 30,	
	2010	**2009**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 20,656	$ 14,204
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of intangible assets	315	898
Depreciation expense	28,910	32,788
Stock-based compensation expense restricted stock and stock units	28,969	30,128
Stock-based compensation expense stock options	155	558
Excess tax benefits from stock-based compensation	(709)	(1,777)
Provision for deferred income taxes	(7,182)	1,813
Provision for doubtful accounts	2,101	(1,449)
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable	(35,275)	116,824
Decrease in accounts payable, accrued expenses, accrued payroll costs and retirement obligations	(1,555)	(69,400)
Increase (decrease) in income taxes payable	7,899	(5,397)
Change in other assets, net of change in other liabilities	6,700	6,315
Net cash flows provided by operating activities	50,984	125,505
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(14,412)	(24,148)
Decrease (increase) in trusts for employee benefits and retirement plans	609	(1,254)
Net cash flows used in investing activities	(13,803)	(25,402)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repurchases of common stock	(71,761)	(57,671)
Cash dividends paid	(38,634)	(36,287)
Decrease in notes payable and other indebtedness	(55)	(51)
Excess tax benefits from stock-based compensation	709	1,777
Proceeds from exercises of stock options	5,385	17,907
Net cash flows used in financing activities	(104,356)	(74,325)
Effect of exchange rate changes on cash and cash equivalents	(8,575)	< Third Quarter ended September 30, 2002 $ 1.88 $ 1.45

Second Quarter ended June 30, 2002	$ 2.03	$ 1.44
First Quarter ended March 31, 2002	$ 2.49	$ 1.70

EQUITY COMPENSATION PLAN INFORMATION

The following table provides information about our Equity Compensation Plans.

Plan Category	Number of securities to be issued upon exercise of outstanding options	Weighted average price of outstanding options	Number of securities remaining available for future issuance
Long Term Incentive plan approved by security holders	875,000	$6.80	848,000
Long Term Incentive plan not approved by security holders			
Directors and Officers plan approved by security holders	140,000	$3.63	160,000
Directors and Officers plan not approved by security holders			
Other equity compensation plan approved by security holders	4,000,000	$5.00	
Other equity compensation plan not approved by security holders			

APPROXIMATE NUMBER OF EQUITY SECURITYHOLDERS

On February 14, 2005, Flanders' common stock closed at $10.50. As of February 14, 2005, there were approximately 153 holders of record of the Company's common stock. The Company estimates there are approximately 3 beneficial owners (holders of more than 5% of the common stock) of the Company s common stock.

DIVIDENDS

We have not declared or paid cash dividends on our common stock. Currently, we retain any future earnings, except those used to repurchase stock, to finance the growth and development of the business, however, we are currently considering paying cash dividends in the future. The Board of Directors may decide to declare a dividend, based upon its evaluation of our earnings, financial position, capital requirements and any other factors the Board of Directors may consider to be relevant. Under the terms of our revolving credit line we cannot pay dividends without the prior written consent of the bank. The Company also has a stock repurchase program that is currently subject to restriction under the Company s line of credit facility. See Management s Discussion and Analysis of Financial Condition and

Results of Operations - Liquidity and Capital Resources and Notes to Consolidated Financial Statements - Note G.

SALES OF UNREGISTERED SECURITIES

The Company did not sell any unregistered securities during 2004, 2003 or 2002.

Item 6.

Selected Financial Data

The following financial data is derived from, and should be read in conjunction with, the Consolidated Financial Statements and notes thereto. Information concerning significant trends in the financial condition and results of operations is contained in Management s Discussion and Analysis of Financial Condition and Results of Operations.

SELECTED HISTORICAL OPERATIONS DATA (In thousands, except per share data)

				Year Ended December 31,	
	2004	2003	2002	2001	2000
	$	$	$	$	$
Net sales	199,933	182,780	184,211	189,077	194,072
Gross profit	48,288	43,271	40,821	39,782	36,917
Operating expenses	33,569	32,112	29,591	36,311	40,733
Operating income (loss) from continuing operations	14,719	11,159	11,230	3,471	(3,816)
Earnings (loss) from continuing operations before income taxes	14,351	11,251	7,740	1,489	(6,940)
Provision (benefit) for income taxes	4,581	3,505	3,001	930	(2,443)
Earnings (loss) from continuing operations	9,770	7,746	4,739	559	(4,497)
Loss from discontinued operations				(175)	(2,702)
Cumulative effect of accounting change			(27,681)		
		$	$	$	$
Net earnings (loss)	9,770	7,746	(22,942)	384	(7,199)

Earnings (loss) per share from continuing operations					
Basic	$ .37	$ 0.30	$ 0.18	$ 0.02	$ (0.18)
Diluted	$ .36	$ 0.29	$ 0.18	$ 0.02	$ (0.18)
Net earnings (loss) per share					
Basic	$ .37	$ 0.30	$ (0.88)	$ 0.01	$ (0.28)
Diluted	$ .36	$ 0.29	$ (0.88)	$ 0.01	$ (0.28)
Weighted average common shares outstanding					
Basic	26,201	26,033	26,033	26,036	25,298
Diluted	27,289	26,428	26,033	26,038	26,298

SELECTED HISTORICAL BALANCE SHEET DATA (In thousands)

				December 31,	
	2004	2003	2002	2001	2000
Working capital	$ 54,212	$ 45,547	$ 41,389	$ 14,603	$ 13,644
Total assets	159,670	145,415	141,671	180,255	180,222
Long-term obligations1	23,059	26,290	35,475	52,045	49,370
Total shareholders equity	93,161	80,709	72,928	96,879	98,151

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Long-term obligations include long-term notes payable, long-term debt, including current maturities, convertible debt, and committed capital.

Item 7.

Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with Item 6 Selected Financial Data and our Consolidated Financial Statements, all included herein. The information set forth in this Management s Discussion and Analysis of Financial Condition and Results of Operations includes forward-looking statements that involve risks and uncertainties. Many factors, including but not limited to those discussed below under Factors That May Affect Future Results could cause actual results to differ materially from those contained in these forward-looking statements.

OVERVIEW

Flanders is a full-range air filtration product company engaged in designing, manufacturing and marketing air filtration products and certain related products and services. Our focus has evolved from expansion through acquisition to increasing the quality and efficiency of our high-volume replacement filtration products, and using these benefits to compete more effectively in the marketplace. We also design and manufacture much of our own production equipment as well as glass-based media for many of our air filtration products.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The following discussion and analysis is based upon our consolidated financial statements which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of our financial statements requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses, and assets and liabilities during the periods reported. Estimates are used when accounting for certain items such as revenues, allowances for returns, early payment discounts, customer discounts, doubtful accounts, employee compensation programs, depreciation and amortization periods, taxes, inventory values, insurance programs, and valuations of investments, goodwill, other intangible assets and long-lived assets. We base our estimates on historical experience, where applicable, and other assumptions that we believe are reasonable under the circumstances. Actual results may differ from our estimates under different assumptions or conditions. We believe that the following critical accounting policies affect our more significant judgments and estimates used in preparation of our consolidated financial statements.

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. We base our estimates on the aging of our accounts receivable balances and our historical write-off experience, net of recoveries. If the financial condition of our customers were to deteriorate, additional allowances may be required.

We value our inventories at the lower of cost or market. We write down inventory balances for estimated obsolescence or unmarketable inventory equal to the difference between the cost of the inventory and the estimated

market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required.

Estimates of our insurance costs are developed by management s evaluation of the likelihood and probable amount of potential claims based on historical experience and evaluation of each claim. Changes in the key assumptions may occur in the future, which would result in changes to related insurance costs.

Goodwill is reviewed for possible impairment at least annually or more frequently upon the occurrence of an event or when circumstances indicate that the Company s carrying amount is greater than the fair value. The Company adopted the provisions of Statement of Financial Accounting Standard (SFAS) No. 142, Goodwill and Other Intangible Assets (SFAS 142) as of January 1, 2002. In accordance with SFAS 142, the Company examined goodwill for impairment and determined that the Company s carrying amount exceeded the fair value.

During the fourth quarter of 2002, the Company completed its transitional impairment analysis. An independent third party performed valuations of the Company. The third party performing the valuation concluded, based on various methodologies, that the fair value of the Company exceeded its carrying value, and thus, there was no goodwill impairment. In addition, the Company s independent certifying accountants, in accordance with SAS 73 (Using the Work of a Specialist), evaluated the professional qualifications of the third party evaluator, gained an understanding of the work performed, which included an understanding of the specialist s work, methods, and assumptions used and made appropriate tests of data provided to the specialists. The independent certifying accountants concluded that the specialist s findings were supported by the data provided. However, according to SFAS 142, quoted market prices in active markets are the best evidence of fair value, and thus the Company, with the concurrence of the Company s independent certifying accountants, concluded that the higher fair value, as determined by the third party valuation, is not sufficient to outweigh the presumption of fair value indicated by the quoted market price of the Company. Accordingly, the Company determined that an impairment charge upon the adoption of SFAS 142 on January 1, 2002 was necessary.

Generally, sales are recognized when shipments are made to customers. Rebates, allowances for damaged goods and other advertising and marketing program rebates are accrued pursuant to contractual provisions and included in accrued expenses. An insignificant amount of our revenues fall under the percentage-of-completion method of accounting used for long-term contracts. Under this method, sales and gross profit are recognized as work is performed based on the relationship between actual costs incurred and total estimated costs at completion. Sales and gross profit are adjusted prospectively for revisions in estimated total contract costs and contract values. Estimated losses are recorded when identified.

RESULTS OF OPERATIONS (thousands omitted, except per share amounts)

2004 Compared to 2003

The following table summarizes the Company s results of operations as a percentage of net sales for 2004 and 2003.

	2004		2003	
Net sales	$ 199,933	100.0%	$ 182,780	100.0%
Gross profit	48,288	24.2	43,271	23.7
Operating expenses	33,569	16.8	32,112	17.6
Operating income	14,719	7.4	11,159	6.1
Nonoperating income (expense)	(368)	(.2)	92	.1
Earnings before income taxes	14,351	7.2	11,251	6.2
Provision for income taxes	4,581	2.3	3,505	1.9
Net earnings (loss)	$ 9,770	4.9	$ 7,746	4.2

Net Sales: Net sales for 2004 increased by $17,153 or 9.4%, to $199,933, from $182,780 for 2003. The increase in net sales was due to our success in increasing our market share across generally all lines of our business.

Gross Profit: Gross profit for 2004 increased $5,017 or 11.6%, to $48,288 which made up 24.2% of net sales, from $43,271 for 2003, which made up 23.7% of net sales. The gross profit increase was principally due to a higher sales volume and cost reductions attributable to:

- Reductions in raw material expenses due to in-house production of various raw materials.
- Reductions in direct labor force headcount and better utilization of our automated equipment.

Operating Expenses: Operating expenses for 2004 increased $1,457, or 4.5%, to $33,569, from $32,112 in 2003. The increase in operating expenses was primarily caused by a higher sales volume in 2004. Operating expenses as a percentage of sales decreased in 2004 to 16.8% from 17.6% due primarily to a reduction of bad debt expense from

2003 of approximately $3.5 million in 2003 to$2.0 million in 2004.

Nonoperating income (expense): Nonoperating income (expense) decreased approximately $460 to ($368) of expense for 2004, compared to $92 of income in 2003. The decrease was due to a reduction of other income partially offset by a reduction of interest exepnse of approximately $300.

Provision for Income Taxes: Our effective state and federal tax rate, adjusted for the effect of certain one-time credits and adjustments, was approximately 38% and 39% for 2004 and 2003, respectively.

2003 Compared to 2002

The following table summarizes the Company s results of operations as a percentage of net sales for 2003 and 2002 (dollar amounts in thousands).

	2003		2002	
Net sales	$ 182,780	100.0%	$ 184,211	100.0%
Gross profit	43,271	23.7	40,821	22.2
Operating expenses	32,112	17.6	29,591	16.1
Operating income (loss) from continuing operations	11,159	6.1	11,230	6.1
Nonoperating income (expense) from continuing operations..	92	.1	(3,490)	(1.9)
Earnings (loss) from continuing operations before income taxes	11,251	6.2	7,740	4.2
Provision (benefit) for income taxes	3,505	1.9	3,001	1.6
Earnings (loss) from continuing operations	7,746	4.2	4,739	2.6

Cumulative effect of accounting change		0.0		(27,681)	(15.0)
Net earnings (loss)	$		$		
	7,746	4.2		(22,942)	(12.5)

Net Sales: Net sales for 2003 decreased by $1,431 or .8%, to $182,780, from $184,211 for 2002. The decrease in net sales was due to a general decrease in air filter sales across the industry which began in the fourth quarter of 2001 and the elimination of unprofitable product lines, partially balanced by our success in increasing our market share.

Gross Profit: Gross profit for 2003 increased $2,450, or 6.0%, to $43,271, which made up 23.7% of net sales, from $40,821 for 2002, which made up 22.2% of net sales. The gross profit increase was principally attributable to:

- Reductions in raw material expenses due to in-house production of various raw materials.
- Reductions in direct labor force headcount and better utilization of our automated equipment.

Operating Expenses: Operating expenses for 2003 increased $2,521, or 8.5%, to $32,112, from $29,591 in 2002. The increase in operating expenses was primarily caused by an unusually high bad debt expense of approximately $3.5 million which management believes is a symptom of the general downturn in the air filtration industry.

Nonoperating income (expense): Nonoperating income (expense) increased approximately $3,582, to $92 of income for 2003, compared to net expense of $3,490 in 2002. The increase was primarily due to a reduction of interest expense of approximately $2.9 million dollars.

Provision for Income Taxes: Our effective state and federal tax rate, adjusted for the effect of certain one-time credits and adjustments in 2003, was approximately 38% and 39% for 2003 and 2002, respectively.

Earnings before cumulative effect of a change in accounting principles: Earnings before cumulative effect of a change in accounting principles for 2003 increased $3,007, to $7,746, or $0.30 per share, from $4,739, or $0.18 per share for 2002. The increase in earnings is primarily attributable to the reduction of interest expense and increase in gross margin due to vertical integration of various raw materials offset by an increase in bad debt expense.

EFFECTS OF INFLATION

The Company s business and operations have not been materially affected by inflation during the periods for which financial information is presented.

LIQUIDITY AND CAPITAL RESOURCES (dollar amounts in thousands)

Working capital was $54,212 at December 31, 2004, compared to $45,547 at December 31, 2003. This included cash and cash equivalents of $1,886 and $1,098 at December 31, 2004 and 2003, respectively. The primary reason for the increase in working capital was cash flows generated from operations net of amounts used to purchase equipment and reduce debt.

Trade receivables increased $5,639, or 15.7% at December 31, 2004 from $35,908 at December 31, 2003. The increase in accounts receivable is attributable to increased sales volume and the aging of various accounts along with the timing differences in shipments and payments received.

Continuing operations generated $8,150 of cash in 2004, compared to $12,313 of cash in 2003. The difference in cash flows was primarily related to increases in inventory and receivables partially offset by higher operating income. Investing activities for continuing operations consumed $7,137 of cash during 2004, compared to consuming $5,010 during 2003, consisting primarily of the purchase of property and equipment. Financing activities for continuing operations consumed $225 and $9,011 of cash in 2004 and 2003, respectively, consisting primarily of payments on long-term debt.

On October 17, 2002, we signed agreements for a new credit facility with Fleet Capital Corporation, which replaced and repaid our previous $30 million revolving credit facility. The new $40 million facility consists of a $7 million term loan and a $33 million revolving credit line, both of which expire on October 17, 2007. The term loan bears interest, at our option, at either (i) LIBOR plus between 2.5% and 3%, dependent on the Company s fixed charge coverage during the prior twelve months; or (ii) the greater of the Federal Funds Effective Rate plus 0.5% or Fleet s base rate, plus between 0.5% and 1%, dependent on the Company s fixed charge coverage during the prior twelve months. The $33 million revolving credit facility bears interest at 0.25% less than the term loan. Up to $11 million of the revolving credit facility may be used to issue letters of credit. The facility is collateralized by substantially all of

the Company s assets. The line of credit agreement requires maintenance of certain financial ratios, and restricts capital expenditures, dividends and share repurchases. Unless this credit facility is renewed, it will expire on October 17, 2007. There are no prepayment penalties on any of the credit facilities with Fleet Capital Corporation.

In connection with the amended working capital credit facility and notes payable to a regional development authority and bank, the Company has agreed to certain restrictive covenants which include, among other things, restricting capital expenditures to less than $7,500 for 2004 and $3,250 per year, thereafter, not paying dividends or repurchasing its stock without prior written consent, and maintenance of certain financial ratios at all times including: a minimum current ratio, minimum tangible net worth, a maximum ratio of total liabilities to tangible net worth and a minimum fixed charge coverage ratio.

As of December 31, 2004 we had the following fixed obligations and commitments:

Year ended December 31,	**Operating leases**	**Capital leases**	**Long-term debt**	**Other long-term obligations**
2005	2,253	434	2,119	
2006	1,034	467	1,894	
2007	491	506	3,267	
2008	145	540	336	
2009	125	589	359	
Thereafter	125	266	12,282	1,729

We believe that our cash on hand, cash generated by operations, and cash available from our existing credit facilities is sufficient to meet the capital demands of our current operations during the 2005 fiscal year. Any major increases in sales, particularly in new products, may require substantial capital investment for the manufacture of filtration products. Failure to obtain sufficient capital could materially adversely impact our growth potential.

We are currently considering paying cash dividends in the future to holders of our common stock. Under the terms of our revolving credit line we cannot pay dividends without the prior written consent of the bank.

In 1998, the Board of Directors authorized the repurchase of up to two million shares of our common stock, which repurchase was completed in September 2000. On September 22, 2000, the Board of Directors authorized the repurchase of up to an additional two million shares of common stock through open market or negotiated transactions. Further repurchases under this program are restricted under our current line of credit agreement, and require prior consent of Fleet Capital Corporation. As of February 14, 2005, approximately 552,000 shares had been repurchased in the open market under this authorization.

Outlook

During 2004 Global Containment Systems, Inc. (GCS) , a wholly owned subsidiary of Flanders Corporation, was formed. GCS will expand its operations into a 400,000 square foot facility in Aiken, SC. This facility will accommodate the requirements for various nuclear containment projects scheduled at the Westinghouse Savannah River Site in Aiken, SC as well as other projects scheduled worldwide over the next ten years. The expansion into South Carolina will provide a state of the art facility with room necessary to provide in place testing, integration, process control verification and final testing and final installation which is expected to provide GCS a unique position in this developing market.

Additionally, during 2004, Flanders Complete Service Division (Flanders CSD), an air filtration service provider was formed. Flanders CSD will offer weekly, monthly and quarterly service contracts for clean room and glove box certification; commercial, industrial, retail and residential surveys; and complete filtration Management including mold remediation and analysis. Based on the breadth of the company s existing manufacturing plants, the company expects to have national coverage by the end of 2005.

During the past three years, we have captured additional market share among big box retailers like The Home Depot and Wal-Mart, capitalizing on our ability to service national accounts from regional distribution centers and our improved on-time delivery performance. We anticipate additional market gains among these types of retailers during the next two years and are introducing new products focused on their marketing and end-user requirements. Sales to these retail outlets, while seasonal, also tend to follow progress in the overall economy. Additional gains in market share in this segment may not have a significant impact on revenues without some recovery in the overall U.S. economy. Additionally, significant revenue enhancement to these customers is largely dependent upon the success of the new products we are introducing to this marketplace.

During the past three years, we introduced air filtration products which use the Arm&Hammer® brand name. We have recently completed development of antimicrobial air filtration products using the Lysol™ brand name. These products are expected to contribute to our expansion in the retail marketplace, but the extent to which they will do so, and their impact on the bottom line, is currently indeterminable.

We have adapted our biocontainment products for use as part of a system for hardening government buildings, commercial office complexes and public venues against airborne bioweapons such as anthrax and smallpox. There is currently an increase of interest in these products over the past quarter. Any interest towards hardening these types of facilities against airborne bioweapons could have a significant impact on our business.

Sales of air filtration products for semiconductor facilities, historically a major market, are expected to be slow again during the first six months of 2005, with most analysts pushing recovery for this sector out to at least the fourth

quarter 2005. However, the strengthening economy is also having a positive effect on sales of all our products.

We have collected data that indicates that residential filter users replace their filters, on average, approximately one and a half times per year. Manufacturers of residential furnace and air conditioning systems recommend that these filters be changed every month. A minor trend toward increased maintenance of these residential heating and cooling systems could have a positive impact on our business.

Our most common products, in terms of both unit and dollar volume, are residential throw-away spun-glass filters, which usually sell for prices under $1.00. Any increase in consumer concern regarding air pollution, airborne pollens, allergens, and other residential airborne contaminants could result in replacement of some of these products with higher value products. Our higher value products include our NaturalAire® higher-efficiency filters for residential use, and our Lysol™ and Arm&Hammer® co-branded products, with associated sales prices typically over $5.00 each. Any such trend would have a beneficial effect on our business.

We believe there is currently a gradually increasing public awareness of the issues surrounding indoor air quality and that this trend will continue for the next several years. We also believe there is an increase in public concern regarding the effects of indoor air quality on employee productivity, as well as an increase in interest by standards-making bodies in creating specifications and techniques for detecting, defining and solving indoor air quality problems. We further believe there will be an increase in interest in our Absolute Isolation Barriers in the future because these products may be used in both semiconductor and pharmaceutical manufacturing plants to prevent cross-contamination between different lots and different processes being performed at the same facility. These products also increase production yields in many applications.

Currently, the largest domestic market for air filtration products is for mid-range ASHRAE-rated products and HVAC systems, typically used in commercial and industrial buildings. To date, our penetration of this market has been relatively small. We believe our ability to offer a one stop supply of air filtration products to HVAC distributors and wholesalers may increase our share of this market. We also believe that our recently developed modular air handlers and environmental tobacco smoke systems will enable us to expand sales to these customers. We intend our new products to serve as high profile entrants with distributors and manufacturers representatives, who can then be motivated to carry our complete product line.

We have continually looked for cost reductions in our products. During the past five years, we have continued to complete the development and redesigning of numerous systems and products which were only partially completed when we acquired the companies which originally claimed to have fully developed them. These products include the automated machinery necessary for high-speed production of our pleated filters, acquired with Precisionaire, and the mass-production processes for bonded carbon high-mass zero-density products. During 2005, we are expecting to move from semi automated lines to fully automated production lines which is expected to significantly reduce our labor related costs

This Outlook section, and other portions of this document, include certain forward-looking statements within the meaning of that term in Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934, including, among others, those statements preceded by, following or including the words believe, expect, intend, anticipate or similar expressions. These forward-looking statements are based largely on the current expectations of management and are subject to a number of assumptions, risks and uncertainties. Our actual results could differ materially from these forward-looking statements. Important factors to consider in evaluating such forward-looking statements include those discussed below under the heading Factors That May Affect Future Results as well as:

- the shortage of reliable market data regarding the air filtration market,
- changes in external competitive market factors or in our internal budgeting process which might impact trends in our results of operations,
- anticipated working capital or other cash requirements,
- changes in our business strategy or an inability to execute our strategy due to unanticipated changes in the market,
- product obsolescence due to the development of new technologies, and
- various competitive factors that may prevent us from competing successfully in the marketplace.

In light of these risks and uncertainties, there can be no assurance that the events contemplated by the forward-looking statements contained in this Form 10-K will in fact occur.

Factors That May Affect Future Results

Failure to Manage Future Growth Could Adversely Impact Our Business Due to the Strain on Our Management, Financial and Other Resources

If our business expands in the future, the additional growth will place burdens on management to manage such growth while maintaining profitability. Our ability to compete effectively and manage future growth depends on our ability to:

- recruit, train and manage our work force, particularly in the areas of corporate management, accounting, research and development and operations,
- manage production and inventory levels to meet product demand,
- manage and improve production quality,
- expand both the range of customers and the geographic scope of our customer base, and
- improve financial and management controls, reporting systems and procedures.

Any failure to manage growth effectively could have a material adverse effect on our business, financial condition and results of operations.

Any Delay in Procuring Financing for New Products or Failure to Adequately Ramp-Up Production Capacity to Meet Demand Could Adversely Impact Our Business Due to Strain on Financial Resources.

During 2005 and 2006, we plan to introduce and market various products which, if successful, may require additional financing and/or capital. This financing may need to be available on short notice. Any failure to obtain such financing, or delay in financing, could cause the failure of the new products due to inability to deliver on time, and could adversely impact relationships with current major accounts. In addition, delays in an untried supply chain, new production chains, and other delays common to the launch of a new product line could also adversely impact the success of the products, as well as current relationships with major accounts.

Our Business May Suffer If Our Competitive Strategy is Not Successful

Our continued success depends on our ability to compete in an industry that is highly competitive. This competition may increase as new competitors enter the market. Several of our competitors may have longer operating histories and greater financial, marketing and other resources than we do. Additionally, our competitors may introduce new products or enhancements to products that could cause a decline in sales or loss of market acceptance of our existing products. Under our current competitive strategy, we endeavor to remain competitive by:

- increasing our market share,
- expanding our market through the introduction of new products which require periodic replacement, and
- improving operating efficiencies.

Although our executive management team continues to review and monitor our strategic plans, we have no assurance that we will be able to follow our current strategy or that this strategy will be successful.

Our Market Share May Not Continue to Increase if We are Unable to Acquire Additional Synergistic Businesses

In the past several years, we have significantly increased our market share by acquiring synergistic businesses. Although we intend to continue to increase our market share in this manner, we have no assurance that future acquisition opportunities will be available, and do not anticipate that future acquisitions will be of a size which would result in immediate significant increases in the size of our business. Additionally, in the future we may not have access to the substantial debt or equity financing to finance potential acquisitions. Moreover, these types of transactions may result in potentially dilutive issuances of equity securities, the incurrence of additional debt and other acquisition-related expenses, all of which could adversely affect our profitability or cash flows. Our strategy of growth through acquisition also exposes us to the potential risks inherent in assessing the value, strengths, weaknesses, and potential profitability of acquisition candidates and in integrating the operations of acquired companies. We do not currently have any binding agreements with respect to future acquisitions.

Our Business May Suffer if Our Strategy to Increase the Size and Customer Base of the Air Filtration Market is Unsuccessful

We are developing new products as part of our strategy to increase the size and customer base of the air filtration market. We have no assurance that this strategy will be successful. We have no guarantee that any new products we develop will gain acceptance in the marketplace, or that these products will be successful. Additionally, we have no assurance we will be able to recoup the expenditures associated with the development of these products. To succeed in this area we must:

- increase public awareness of the issues surrounding indoor air quality,
- adequately address the unknown requirements of the potential customer base,
- develop new products that are competitive in terms of price, performance and quality, and
- avoid significant increases in current expenditure levels in development, marketing and consumer education.

We May Experience Critical Equipment Failure Which Could Have a Material Adverse Effect on Our Business

If we experience extended periods of downtime due to the malfunction or failure of our automated production equipment, our business, financial condition and operations may suffer. We design and manufacture much of the automated production equipment used in our facilities. We also use other technologically advanced equipment for which manufacturers may have limited production capability or service experience. If we are unable to quickly repair our equipment or quickly obtain new equipment or parts from outside manufacturers, we could experience extended periods of downtime in the event of malfunction or equipment failure.

Our Plan to Centralize Overhead Functions May Not Produce the Anticipated Benefits to Our Operating Results

We are currently completing the implementation of plans to centralize overhead functions and eliminate duplication of efforts between our subsidiaries in the following areas:

- purchasing,
- production planning,
- shipping coordination,
- marketing,
- accounting,
- personnel management,
- risk management, and
- benefit plan administration.

We have no assurance that cutting overhead in this fashion will have the anticipated benefits to our operating results. Additionally, we have no assurance that these reorganizations will not significantly disrupt the operations of the

affected subsidiaries.

Our Success Depends on Our Ability to Retain and Attract Key Personnel

Our success and future operating results depend in part upon our ability to retain our executives and key personnel, many of whom would be difficult to replace. Our success also depends on our ability to attract highly qualified engineering, manufacturing, technical, sales and support personnel for our operations. Competition for such personnel, particularly qualified engineers, is intense, and there can be no assurance that we will be successful in attracting or retaining such personnel. Our failure to attract or retain such persons could have a material adverse effect on our business, financial condition and results of operations.

Our Current Distribution Channels May be Unavailable if Our Manufacturers Representatives Decide to Work Primarily With One of Our Competitors

We provide our manufacturers representatives with the ability to offer a full product line of air filtration products to existing and new customers. Some of our competitors offer similar arrangements. We do not have exclusive relationships with all of our representatives. Consequently, if our representatives decide to work primarily with one of our competitors, our current distribution channels, and hence, our sales, could be significantly reduced.

Management Controls a Significant Percentage of Our Stock

As of December 31, 2004, our directors and executive officers beneficially held approximately 51.43% of our outstanding common stock. As a result, such shareholders effectively control or significantly influence all matters requiring shareholder approval. These matters include the election of directors and approval of significant corporate transactions. Such concentration of ownership may also have the effect of delaying or preventing a change in control that may otherwise be advantageous to the non-affiliated shareholders.

We May be Required to Issue Stock in the Future That Will Dilute the Value of Our Existing Stock

We have granted options to purchase a total of 5,000,000 shares of common stock to various parties with exercise prices ranging from $1.50 to $8.60 per share. The majority of these options are currently exercisable. Additionally, if the option holders exercise their options, the interests of current shareholders may be diluted.

Our Shareholders May Not Realize Certain Opportunities Because of Our Charter Provisions and North Carolina Law

Our Articles of Incorporation and Bylaws contain provisions that are designed to provide our Board of Directors with time to consider whether a hostile takeover offer is in our best interest and the best interests of our shareholders. These provisions may discourage potential acquisition proposals and could delay or prevent a change of control in our business. Additionally, we are subject to the Control Shares Acquisition Act of the State of North Carolina. This act provides that any person who acquires control shares of a publicly held North Carolina corporation will not have voting rights with respect to the acquired shares unless a majority of the disinterested shareholders of the corporation vote to grant such rights. This could deprive shareholders of opportunities to realize takeover premiums for their shares or other advantages that large accumulations of stock would typically provide.

Our Business Can be Significantly Affected by Environmental Laws

The constantly changing body of environmental laws and regulations may significantly influence our business and products. These laws and regulations require that various environmental standards be met and impose liability for the failure to comply with such standards. While we endeavor at each of our facilities to assure compliance with environmental laws and regulations, and are currently not aware of any ongoing issues of this nature, we cannot be certain that our operations or activities, or historical operations by others at our locations, will not result in civil or criminal enforcement actions or private actions that could have a materially adverse effect on our business. We have, in the past, and may, in the future, purchase or lease properties with unresolved potential violations of federal or state environmental regulations. In these transactions, we have been successful in obtaining sufficient indemnification and mitigating the impact of the issues without recognizing significant expenses associated with litigation and cleanup. However, purchasing or leasing these properties requires us to weigh the cost of resolving these issues and the likelihood of litigation against the potential economic and business benefits of the transaction. If we fail to correctly identify, resolve and obtain indemnification against these risks, they could have a material adverse impact on our financial position.

Because of the foregoing factors, as well as other variables affecting our operating results, past financial performance should not be considered a reliable indicator of future performance, and investors should not use historical trends to anticipate results or trends in future periods.

Item 7A.

Quantitative and Qualitative Disclosures About Market Risk (dollar amounts in thousands)

We are exposed to various market risks, primarily changes in interest rates. Market risk is the potential loss arising from adverse change in market rates and prices, such as foreign currency exchange and interest rates. For Flanders,

these exposures are primarily related to changes in interest rates. We do not hold any derivatives or other financial instruments for trading or speculative purposes.

The fair value of the Company s total long-term debt, including capital leases and current maturities of long-term debt, at December 31, 2004 was $23,059. Market risk was estimated as the potential decrease (increase) in future earnings and cash flows resulting from a hypothetical 10% increase (decrease) in the Company s estimated weighted average borrowing rate at December 31, 2004. Although most of the interest on the Company s debt is indexed to a market rate, there would be no material effect on the future earnings or cash flows related to the Company s total debt for such a hypothetical change.

We have only a limited involvement with derivative financial instruments. We have two interest-rate swap agreements to hedge against the potential impact on earnings from increases in market interest rates of two variable rate bonds. Under the interest rate swap agreements, we receive or make payments on a monthly basis, based on the differential between 5.14% and a tax exempt interest rate as determined by a remarketing agent. This interest rate swap is accounted for as a cash flow hedge in accordance with SFAS 133 and SFAS 138. Gains or losses related to inefficiencies of the cash flow hedge were included in net income during the period related to hedge ineffectiveness. The tax affected fair market value of the interest rate swap of $1,037 is included in Accumulated other comprehensive loss on the balance sheet. The interest rate swap contracts expire in 2013 and 2015.

The Company s financial position is not materially affected by fluctuations in currencies against the U.S. dollar, since assets held outside the United States are negligible. Risks due to changes in foreign currency exchange rates are negligible, as the preponderance of our foreign sales occur over short periods of time or are demarcated in U.S. dollars.

Item 8.

Financial Statements and Supplementary Data

Beginning at page F-1.

Item 9A.

Controls and Procedures

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-(f) promulgated under the Exchange Act as a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and effected by the Company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2004. In making this assessment, the Company's management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

Based on our assessment, management believes that, as of December 31, 2004, the Company's internal control over financial reporting is effective based on those criteria.

The Company's independent auditors have issued an audit report on our assessment of the Company's internal control over financial reporting.

PART III

Item 10.

Directors and Executive Officers of the Registrant

IDENTIFICATION OF DIRECTORS AND EXECUTIVE OFFICERS

Set forth below is information regarding (i) the current directors of the Company, who will serve until the next annual meeting of shareholders or until their successors are elected or appointed and qualified, and (ii) the current executive officers of the Company, who are elected to serve at the discretion of the Board of Directors.

Name

Age

Title

Steven K. Clark

52

Chief Executive Officer and Director

James L. Buddy Mercer

60

Vice President Operations

John W. Hodson

42

Chief Financial Officer

Robert Amerson

54

Chairman of the Board

Robert Kelly Barnhill. Sr.

65

Independent Director

William D. Mitchum, Jr.

57

Independent Director

David M. Mock

52

Independent Director

Peter Fredericks

46

Independent Director

Steven K. Clark. Mr. Clark was the Chief Financial officer and Director from December 1995 through December of 2004. He became the Chief Executive officer in December 2004. Mr. Clark acted as a consultant from November, 1995 through December, 1995. From July 1992 through October 1995, he was the Chief Financial Officer of Daw

Technologies, Inc., a specialty cleanroom contractor and customer of the Company. Prior to this he was a senior partner of Miller and Clark, an accounting and management services firm. Mr. Clark spent four years with Price Waterhouse, and an additional four years with Arthur Andersen, both accounting firms. He is a Certified Public Accountant, has Bachelor of Arts degrees in Accounting and Political Science and a Master of Business Administration Degree, all from the University of Utah.

James L. Buddy Mercer. Mr. Mercer has been Vice President Operations for the Company since December 2001. He has direct responsibility for all plant manufacturing operations. Prior to December 2001, beginning in 1998, he was a general manager for Precisionaire, a subsidiary of the Company. From 1967 through 1997, Mr. Mercer worked at Purolator Air Products, a competitor, working in several positions, up through plant manager.

John W. Hodson. Mr. Hodson has been the Chief Financial Officer of Precisionaire, Inc. and several other Flanders Subsidiaries since October 1999. He became the Chief Financial Officer of Flanders Corporation in December of 2004. He has direct responsibility for overseeing the Corporate accounting department, the financial reporting process and the day to day financial operations of the company. From 1986 through October 1999 he worked primarily as a public accountant for various CPA firms including Price Waterhouse and several smaller firms. He is a Certified Public Accountant in the states of Florida and North Carolina and has a Bachelors degree in Accounting from the University of Central Florida.

Robert Amerson. Mr. Amerson has been President and Chief Executive Officer of the Company since 1987 but retired from these positions in December of 2004 and now Mr. Amerson is the Chairman of the Board of Directors. He has held a director position since 1988. Mr. Amerson has a Bachelor of Science degree in Business Administration from Atlantic Christian College.

Robert Kelly Barnhill, Sr. Mr. Barnhill was appointed as a director in December of 2004. Mr. Barnhill is President of Hendrix-Barnhill Co. Inc., a licensed contractor specializing in the construction of public utilities. Mr. Barnhill has served on the Board of Governors of Greenville Country Club and is the former President of the University City Kiwanis Club. Mr. Barnhill also served as the Pitt County Commissioner and currently serves on the North Carolina Licensing Board for General Contractors, the North Carolina State Engineering Foundation, and is the Vice Chairman of the Pitt Memorial Hospital Foundation. Mr. Barnhill received his degree in Civil Engineering from the North Carolina State University.

William D. Mitchum, Jr. Mr. Mitchum was appointed as a director in December of 2004. Mr. Mitchum is the President and Chief Executive Officer of Mercer Glass Co., Inc., duties he has held since 1981. Prior to this he was the Executive Vice President of Hardware Suppliers of America, Inc. and Eastern Millwork. Mr. Mitchum has served as Director of Local Board BB&T and Local Board First Union National. He is currently Director of Regional Advisory Board Wachovia Bank. Mr. Mitchum received his Bachelor of Science and MBA degrees from East

Carolina University.

David M. Mock. Mr. Mock was appointed as a Director in August 2003 and affirmed by the shareholders in December 2003. Mr. Mock is a general partner with GMG Capital Partner, a New York-based investment firm, which he co-founded in 1997. Prior to joining GMS/GMG Partners, Mr. Mock was a private investor pursuing an investment strategy similar to that of GMG. Mr. Mock is currently Chairman of the Board of Captus Networks as well as serving as Director or Executive Officer to several other companies including Alloptic, Inc., Forum Systems, and Connecting Point, Inc. Mr. Mock holds an Bachelor of Arts Degree in Accounting from the University of Utah and is considered an audit committee financial expert.

Peter Fredericks. Mr. Fredericks has been an independent director since April 2002. Mr. Fredericks is a private equity investor, and has been involved in business management, equity investment, and consulting since 1982. Mr. Fredericks experience includes working as a strategy consultant with the Boston Consulting Group. Mr. Fredericks received his Bachelor of Arts degree in Economics with distinction from Stanford University, his Masters in Business Administration from Harvard University, where he was a Baker Scholar, and his Ph.D. from the Vienna University of Economics and Business Administration.

Item 11.

Executive Compensation

SUMMARY COMPENSATION TABLE

The following table sets forth the aggregate cash compensation paid by the Company for services rendered during the last three years to the Company s Chief Executive Officer and to each of the Company s other executive officers whose annual salary, bonus and other compensation exceeded $100,000 in 2004.

	Annual Compensation			Long-Term Compensation			
				Awards			Payouts
			Other	Restricted	Securities Underlying		
			Annual	Stock	Options/		LTIP
			Compen-	Award(s)	SARs		Payouts
Year	Salary ($)	Bonus($)	sation ($)	($)	(#)		($)

Name and Principal Position				
Steven K. Clark	2004	250,000	11,041	500,000
Chief Executive Officer	2003	254,808	1,587	
	20021	249,519	1,348	
Robert Amerson	2004	259,615		
Chairman of the Board of Directors	2003	246,672		
	20021	249,039	1,231	
John W. Hodson	2004	107,154	4,050	40,000
Chief Financial Officer				
James L. Buddy Mercer	2004	118,247		40,000
Vice President Operations	2003	120,521		80,000
	2002	112,608		

1

Mr. Amerson and Mr. Clark each had an annual salary of $250,000, plus a possible bonus each year, under their respective Employment Agreements, as amended.

AGGREGATED OPTION/SAR EXERCISES IN LAST FISCAL YEAR

AND FISCAL YEAR-END OPTION/SAR VALUES

The following table sets forth the aggregate number and value of stock options and SAR s at year end by the Company s Chief Executive Officer and by each of the Company s other executive officers whose annual salary, bonus and other compensation exceeds $100,000.

Name	Shares Acquired On Exercise (#)	Value Realized ($)	Number of Securities Underlying Unexercised Options/SARs at Fiscal Year-End (#) Exercisable/Unexercisable	Value of Unexercised In-the-Money Options/ SARs at Fiscal Year-End Exercisable/Unexercisable
Steven K. Clark		$	2,500,000 /	$

				9,700,000 /
				$
		$	2,000,000 /	9,200,000 /
Robert R. Amerson				
				$
		$	50,000 /	179,800 /
John W. Hodson	15,000	90,250	80,000	557,600
		$	40,000 /	107,800 /
James L. Buddy Mercer			80,000	516,800

COMPENSATION OF DIRECTORS

Directors who are Company employees receive no additional or special remuneration for serving as Directors. The Company s non-employee Directors are paid $500 plus out-of-pocket expenses for each meeting of the Board of Directors. After being a Director for at least six months, each non-employee Director receives an automatic option to purchase 5,000 shares of the Company s common stock on the first business day at the beginning of the following year. Each current non-employee Director serving also received an option to purchase 50,000 shares of common stock upon their appointment to the Board.

EMPLOYMENT AGREEMENTS

Messrs. Amerson and Clark have employment agreements effective as of December 15, 1995 (Employment Agreements). The Employment Agreements, as amended, provide for an annual base salary of $250,000 for both Mr. Amerson and Mr. Clark and terminate in 2010. The Employment Agreements also provide that the executive shall be entitled to the following termination payments: (i) 100% of his current base salary if the employment is terminated as a result of his death or disability; (ii) up to 200% of his current base salary if the employment is terminated by the Company for any reason other than death, disability or for cause, or (iii) up to 250% of the executive s gross income during the year preceding his termination if the Employment Agreement is terminated by the executive for good reason or by the Company for any reason other than death, disability or cause and the termination occurs within two years after a change of control of the Company has occurred.

Messr. Hodson has a two year employment contract dated January 1, 2005. The employment contract for Hodson provides for an annual base salary of 100K and a discretionary bonus. The Employment Agreement also provides for 200% of his base salary upon termination by the company for any reason other than death or disability.

OTHER INFORMATION REGARDING THE BOARD OF DIRECTORS

Board Meetings and Committees

During 2004, the Board of Directors met four times and also executed various consent resolutions and written actions in lieu of meetings. Additionally, all directors were present, either in person or by proxy, at the Fiscal 2003 Annual Meeting of the Shareholders held in December of 2004.

The Board of Directors currently has an Audit Committee and a Compensation Committee. The Audit Committee reviews the results and scope of the audit and other services provided by the Company s independent auditors, reviews and evaluates the Company s internal audit and control functions, monitors transactions between the Company and its employees, officers and directors, and completes other functions as required by the Public Company Accounting Reform and Investor Protection Act (the Sarbanes-Oxley Act) passed in 2002. David Mock is considered the audit committee financial expert. The Compensation Committee administers the Company s equity incentive plans and designates compensation levels for executive officers and directors of the Company. The Audit Committee met four times during 2004. The Compensation Committee met one time during 2004.

Currently, the Audit Committee consists of Messrs. Mock, Fredericks, Barnhill, and Mitchum, with Mr. Mock serving as Chair. The Compensation Committee consists of Messrs. Fredericks, Mock, Clark and Amerson. Mr. Fredericks serves as Chair and Mr. Clark and Mr. Amerson serve as non-voting advisory members.

Long-Term Incentive Plan

During 1996, the Company adopted the Long Term Incentive Plan (LTI Plan) to assist the Company in securing and retaining key employees and consultants. The LTI Plan authorizes grants of incentive stock options, nonqualified stock options, stock appreciation rights (SARs), restricted stock performance shares and dividend equivalents to officers and key employees of the Company and outside consultants to the Company. There are 1,987,000 shares of Common Stock reserved for award under the LTI Plan. During 2004, 2003 and 2002, the Company awarded options to purchase 630,000, 145,000 and 85,000 shares of Common Stock under the LTI Plan, respectively.

The LTI Plan is administered by the Compensation Committee. The Compensation Committee determines the total number and type of awards granted in any year, the number and selection of employees or consultants to receive awards, the number and type of awards granted to each grantee and the other terms and provisions of the awards, subject to the limitations set forth in the LTI Plan.

Stock Option Grants. The Compensation Committee has the authority to select individuals who are to receive options under the LTI Plan and to specify the terms and conditions of each option so granted (incentive or nonqualified), the exercise price (which must be at least equal to the fair market value of the common stock on the date of grant with respect to incentive stock options), the vesting provisions and the option term. Unless otherwise provided by the Compensation Committee, any option granted under the LTI Plan expires the earlier of five years from the date of grant or, three months after the optionee s termination of service with the Company if the termination of employment is attributable to (i) disability, (ii) retirement, or (iii) any other reason, or 15 months after the optionee s death. As of December 31, 2004, there are 860,000 options outstanding under the LTI Plan.

Stock Appreciation Rights. The Compensation Committee may grant SARs separately or in tandem with a stock option award. A SAR is an incentive award that permits the holder to receive (per share covered thereby) an equal amount by which the fair market value of a share of common stock on the date of exercise exceeds the fair market value of such share on the date the SAR was granted. Under the LTI Plan, the Company may pay such amount in cash, in common stock or a combination of both. Unless otherwise provided by the Compensation Committee at the time of grant, the provisions of the LTI Plan relating to the termination of employment of a holder of a stock option will apply equally, to the extent applicable, to the holder of a SAR. A SAR granted in tandem with a related option will generally have the same terms and provisions as the related option with respect to exercisability. A SAR granted separately will have such terms as the Compensation Committee may determine, subject to the provisions of the LTI Plan. As of December 31, 2004, no SARs are outstanding under the LTI Plan.

Performance Shares. The Compensation Committee is authorized under the LTI Plan to grant performance shares to selected employees. Performance shares are rights granted to employees to receive cash, stock, or other property, the payment of which is contingent upon achieving certain performance goals established by the Compensation Committee. As of December 31, 2004, no performance shares are outstanding under the LTI Plan.

Restricted Stock Awards. The Compensation Committee is authorized under the LTI Plan to issue shares of restricted common stock to eligible participants on such terms and conditions and subject to such restrictions, if any, outstanding under the LTI Plan. As of December 31, 2004, no restricted shares have been awarded under the LTI Plan.

Dividend Equivalents. The Compensation Committee may also grant dividend equivalent rights to participants subject to such terms and conditions as may be selected by the Compensation Committee. Dividend equivalent rights entitle the holder to receive payments equal to dividends with respect to all or a portion of the number of shares of stock subject to an option award or SARs, as determined by the Committee. As of December 31, 2004, no dividend equivalents are outstanding under the LTI Plan.

Section 16(a) Beneficial Ownership Reporting Compliance. Section 16(a) of the Securities Exchange Act of 1934 requires the Company s officers and directors, and persons who own more than ten percent of a registered class of the Company s equity securities, to file reports of ownership and changes in ownership with the Securities and Exchange Commission. Officers and directors are required by SEC regulation to furnish the Company with copies of all Section 16(a) forms filed. Based solely upon review of copies of such forms, or written representations that there were no unreported holdings or transactions, the Company believes that for the fiscal year ending December 31, 2004 all Section 16(a) filing requirements applicable to its officers and directors were complied with on a timely basis except that William Mitchum, Jr. failed to file a Form 3 for 14,100 shares upon becoming a director on April 28, 2004. Mr. Mitchum is in the process of filing a Form 5 to report his stock ownership.

Item 12.

Security Ownership of Certain Beneficial Owners and Management

The following table sets forth all individuals known by the Company to beneficially own 5% or more of the Company s common stock, and all officers and directors of the registrant, with the amount and percentage of stock beneficially owned, as of December 31, 2004. Except as indicated in the following footnotes, each listed beneficial owner has sole voting and investment power over the shares of common stock held in their names.

Name and Address of Beneficial Owner	Shares of Common Stock Beneficially Owned	Percentage of Outstanding Shares of Common Stock [1]
Robert R. Amerson [2] 531 Flanders Filters Road Washington, NC 27889	7,573,370	28.79%
Steven K. Clark [3] 2399 26th Avenue North Saint Petersburg, Florida 33713	5,535,183	21.04%
John W. Hodson(4)	65,000	*

William D. Mitchum, Jr. (5)	14,100	*
David Mock(6)	161,000	*
James L. Buddy Mercer(7)	120,000	*
Robert Kelly Barnhill, Sr.(8)	0	*
Peter Fredericks (9)	59,707	*
Dimensional Fund Advisors Inc.	1,040,716	3.96%
1299 Ocean Avenue, 11th Floor		
Santa Monica, CA 90401		
Officers and Directors as a group	13,528,360	51.43%
(8 persons) (2), (3), (4), (5), (6), (7), (8), (9)		

*

Represents less than 1% of the total issued and outstanding shares of common stock.

(1)

Applicable percentage of ownership is based on 26,303,496 shares of common stock outstanding as of December 31, 2004, together with all applicable options for unissued securities for such shareholders exercisable within 60 days. Shares of common stock subject to options exercisable within 60 days are deemed outstanding for computing the percentage ownership of the person holding such options, but are not deemed outstanding for computing the percentage of any other person.

(2)

Includes 1,000,000 shares which are subject to an option to purchase such shares from the Company at $2.50 per share. These options expire in 2009. Also includes 1,000,000 shares which are subject to an option to purchase such shares from the Company at $7.50 per share. These options expire in 2011.

(3)

Includes 1,000,000 shares which are subject to an option to purchase such shares from the Company at $2.50 per share. These options expire in 2009. Also includes 1,000,000 shares which are subject to an option to purchase such shares from the Company at $7.50 per share. These options expire in 2011. Also includes 500,000 shares which are subject to an option to purchase such shares from the Company at $8.60 per share. These options expire in 2009.

(4)

Includes 10,000 shares which are subject to an option to purchase such shares from the Company at $2.40 per share. These options expire in 2006. Also includes 20,000 shares which are subject to an option to purchase such shares from the Company at $5.21 share. These options expire in 2009. Also includes 20,000 shares which are subject to an option to purchase such shares from the Company at $8.60 per share. These options expire in 2009.

(5)

Director was not issued any options in 2004.

(6)

Includes 50,000 shares which are subject to an option to purchase such shares from the Company at $4.37 per share. These options expire in 2008.

(7)

Includes 60,000 shares which are subject to an option to purchase such shares from the Company at $2.52 per share. Also includes 20,000 shares which are subject to an option to purchase such shares from the Company at $5.00 per share. These options expire in 2008. Also includes 20,000 shares which are subject to an option to purchase such shares from the Company at $5.21 per share. Also includes 20,000 shares which are subject to an option to purchase such shares from the Company at $8.60 per share. These options expire in 2009.

(8)

Director was not issued any options in 2004.

(9)

Includes 35,000 shares which are subject to an option to purchase such shares from the Company at $1.74 per share. These options expire in 2007. Also includes 5,000 shares which are subject to an option to purchase such shares from the Company at $6.49 per share. These options expire in 2009.

Item 13.

Certain Relationships and Related Transactions (dollar amounts in thousands)

At December 31, 2004, Steven K. Clark owed the Company $3,782 of principal and $860 of accrued interest which he previously borrowed to make certain payments under an indemnity agreement he entered into with the Company, to exercise options and to purchase certain shares. This debt is evidenced by a note which bears interest at LIBOR plus 1%, and is due in full on December 31, 2010, or on demand by the Company if he terminates employment, and is secured by common stock.

At December 31, 2004, Robert R. Amerson owed the Company $1,967 of principal and $760 of accrued interest, which he previously borrowed, the majority of which was used to settle claims, to make certain payments under an indemnity agreement he entered into with the Company, to purchase certain shares and for other unspecified reasons. This debt is evidenced by a note which bears interest at LIBOR plus 1%, and is due in full on December 31, 2010, or on demand by the Company if he terminates employment, and is secured by common stock.

On January 2, 2001, the Company purchased and leased back $797 in manufacturing equipment from Superior Diecutting, Inc., a vendor 50% owned by two officer and directors. The Company also loaned this supplier $500, secured by a building and used to pay off an existing mortgage, and $400 to repay a credit line secured by inventory, receivables and other current assets. The Company made payments of $6,933 and $3,738 in 2004 and 2003, respectively, to this supplier for purchases of raw materials. At December 31, 2004 and 2003, the Company owed a total of $2,591 and $892, respectively, to this vendor. At December 31, 2004, Superior Diecutting, Inc. owed the Company $5,880. The accounts and operations of this related entity have been consolidated, thus, the financial effects of these transactions have been eliminated in consolidation.

The Company made payments totaling $1,041 and $1,038 in 2004 and 2003, respectively, to Wal-Pat II, a real estate Limited Liability Company which leases property to the Company. Wal-Pat II is owned by Robert R. Amerson and Steven K. Clark (fifty percent each). At December 31, 2004, the Company owed a total of $0 to Wal-Pat II.

Item 15.

Principal Accountant Fees and Services (dollar amounts in thousands)

Audit Related Fees

Our principal accountants billed us an aggregate of $217 and $170 in fees and expenses for professional services rendered in connection with the audits of our financial statements for the calendar years ended December 31, 2004 and 2003, respectively, and reviews of the financial statements included in our quarterly reports on Form 10-Q during such calendar years.

Our principal accountants did not bill us any additional fees that are not disclosed under audit fees in each of the last two calendar years for assurance and related services that are reasonably related to the performance of our audit or

review of our financial statements.

Tax Fees

Our principal accountants billed us an aggregate of $76 and $53 in fees and expenses for tax compliance, tax advice and tax planning during calendar years ended December 31, 2004 and 2003, respectively.

All Other Fees

Our principal accountants billed us an aggregate of $27 and $7 in fees and expenses during calendar years ended December 31, 2004 and 2003, respectively, for products and services other than those products and services described above. These services consist of the following:

- Audit of profit sharing plan and discussions regarding Sarbanes Oxley 404.

Audit Committee Pre-Approval Process, Policies and Procedures

The appointment of Pender Newkirk & Co. was approved by our Audit Committee and full Board of Directors. Our principal auditors have performed their audit procedures in accordance with pre-approved policies and procedures established by our Audit Committee. Our principal auditors have informed our Audit Committee of the scope and nature of each service provided. With respect to the provisions of services other than audit, review, or attest services, our principal accountants brought such services to the attention of our Audit Committee, or one or more members of our Audit Committee for the members of our Board of Directors to whom authority to grant such approval had been delegated by the Audit Committee, prior to commencing such services. Such services primarily consisted of tax related services.

Code of Ethics for Senior Financial Officers

The code of ethics established by the Company for its Senior Financial Officers is required to be signed by each such officer, is maintained on file by the Company, and incorporates the following:

Senior Financial Officers hold an important and elevated role in corporate governance. While members of the management team, they are uniquely capable and empowered to ensure that all stakeholder s interests are appropriately balanced, protected and preserved. This Code provides principles to which Flanders Corporation Officers are expected to adhere and advocate. They embody rules regarding individual and peer responsibilities, as well as responsibilities to employers, the public and other stakeholders. Our Senior Financial Officers agree by their signature below that they will:

1. Act with honesty and integrity, avoiding actual or apparent conflicts of interest in personal and professional relationships.
2. Will make reasonable efforts to comply with rules and regulations of federal, state, provincial and local governments, and other appropriate private and public regulatory agencies as known to them and will make reasonable efforts to maintain or obtain a professional level of knowledge of applicable rules and regulations.
3. Act in good faith, responsibly, with due care, competence and diligence, without misrepresenting material facts or allowing one s independent judgment to be subordinated.
4. Respect the confidentiality of information acquired in the course of one s work except when authorized or otherwise legally obligated to disclose. Confidential information acquired in the course of one s work will not be used for personal advantage.

PART IV

Item 16.

Exhibits, Financial Statement Schedules and Reports on Form 8-K

The following constitutes a list of Financial Statements, Financial Statement Schedules and Exhibits used in this report.

(a)(1)

Financial Statements: Financial Statements are included beginning at page F-1 as follows:

Report of Independent Certified Public Accountants

F-2

Consolidated Balance Sheets at December 31, 2004 and 2003

F-3

Consolidated Statements of Operations for the years ended December 31, 2004, 2003 and 2002

F-4

Consolidated Statements of Stockholders Equity for the years ended December 31, 2004, 2003and 2002

F-6

Consolidated Statements of Cash Flows for the years ended December 31, 2004, 2003 and 2002

F-7

Notes to Consolidated Financial Statements

F-9

(a)(2)

Financial Statement Schedules

Report of Independent Certified Public Accountants on schedule

F-30

Schedule II. Valuation and Qualifying Accounts

F-31

All schedules not listed have been omitted because they are not applicable or the information has been otherwise supplied in the Registrant s financial statements and schedules.

(a)(3)

Exhibits:

3.1

Articles of Incorporation for Flanders Corporation, filed with the Form 8-A dated March 8, 1996, incorporated herein by reference.

3.2

Bylaws of Flanders Corporation, filed with the Form 8-A dated March 8, 1996, incorporated herein by reference.

10.1

Loan and Security Agreement, dated October 9, 2002, by and among Fleet Capital Corporation, Flanders Corporation, Flanders/Precisionaire Corp., Flanders Filters, Inc., Flanders/CSC Corporation, Precisionaire, Inc., Precisionaire of Utah, Inc., Eco-Air Products, Inc., Air Seal Filter Housings, Inc. and Flanders Realty Corp., filed with the Form 8-K/A dated October 21, 2002.

10.2

First Amendment to Loan and Security Agreement, dated October 18, 2002, by and among Flanders Corporation, Flanders/Precisionaire Corp., Flanders Filters, Inc., Flanders/CSC Corporation, Precisionaire, Inc., Precisionaire of Utah, Inc., Eco-Air Products, Inc., Air Seal Filter Housings, Inc., Flanders Realty Corp. and Fleet Capital Corporation, filed with the Form 8-K/A dated October 21, 2002.

10.3

Second Amendment to Loan and Security Agreement, dated November 19, 2002, by and among Flanders Corporation, Flanders/Precisionaire Corp., Flanders Filters, Inc., Flanders/CSC Corporation, Precisionaire, Inc., Precisionaire of Utah, Inc., Eco-Air Products, Inc., Air Seal Filter Housings, Inc., Flanders Realty Corp. and Fleet Capital Corporation, filed with the Form 8-K/A dated October 21, 2002.

10.3.1

Third Amendment to Loan and Security Agreement, dated Sptember 6, 2003 by and among Flanders Corporation, Flanders/Precisionaire Corp., Flanders Filters, Inc., Flanders/CSC Corporation, Precisionaire, Inc., Precisionaire of Utah, Inc., Eco-Air Products, Inc., Air Seal Filter Housings, Inc., Flanders Realty Corp. and Fleet Capital Corporation.

10.3.2

Fourth Amendment to Loan and Security Agreement, dated December 8, 2003, by and among Flanders Corporation, Flanders/Precisionaire Corp., Flanders Filters, Inc., Flanders/CSC Corporation, Precisionaire, Inc., Precisionaire of Utah, Inc., Eco-Air Products, Inc., Air Seal Filter Housings, Inc., Flanders Realty Corp. and Fleet Capital Corporation.

10.4

Support Agreement and Guaranty dated October 18, 2002, between Fleet Capital Corporation and Steven K. Clark, filed with the Form 8-K/A dated October 21, 2002.

10.5

Support Agreement and Guaranty dated October 18, 2002, between Fleet Capital Corporation and Robert Amerson, filed with the Form 8-K/A dated October 21, 2002.

10.6

Continuing Guaranty Agreement dated October 18, 2002, between Fleet Capital Corporation and Superior Diecutting, Inc., filed with the Form 8-K/A dated October 21, 2002.

10.7

Amended and Restated Continuing Guaranty dated November 26, 2002, between Fleet Capital Corporation and Superior Diecutting, Inc., filed with the Form 8-K/A dated October 21, 2002.

10.8

Loan Agreement between Will-Kankakee Regional Development Authority and Flanders Corporation dated December 15, 1997, filed with the December 31, 1997 Form 10-K, and incorporated herein by reference.

10.9

Loan Agreement between Flanders Corporation and the Johnston County Industrial Facilities and Pollution Control Financing Authority, dated April 1, 1998, filed with the Form 10-Q dated March 31, 1998, and incorporated herein by reference.

10.10

Loan Agreement between Flanders Corporation and the Johnston County Industrial Facilities and Pollution Control Financing Authority, dated March 1, 2000, filed with the Form 10-K dated December 31, 1999, and incorporated herein by reference.

10.11

Flanders Corporation 1996 Director Option Plan, filed with the Form 10-K dated December 31, 1995, and incorporated herein by reference.

10.12

Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc., and Steven K. Clark, filed with the December 31, 1995 Form 10-K, incorporated herein by reference.

10.13

Amendment to Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc., and Steven K. Clark, filed with Form S-1 dated October 21, 1996 (Reg. No. 333-14655) and incorporated herein by reference.

10.14

Amendment to Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc., and Steven K. Clark, filed with the Form 10-K dated December 31, 1997 and incorporated herein by reference.

10.15

Amendment to Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc., and Steven K. Clark, filed with the Form 10-K dated December 31, 1999, and incorporated herein by reference.

10.16

Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc. and Robert R. Amerson, filed with the December 31, 1995 Form 10-K, incorporated herein by reference.

10.17

Amendment to Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc., and Robert R. Amerson, filed with Form S-1 dated October 21, 1996 (Reg. No. 333-14655) and incorporated herein by reference.

10.18

Amendment to Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc., and Robert R. Amerson, filed with the Form 10-K dated December 31, 1997 and incorporated herein by reference.

10.19

Amendment to Employment Agreement between Elite Acquisitions, Inc., Flanders Filters, Inc., and Robert R. Amerson, filed with the Form 10-K dated December 31, 1999, and incorporated herein by reference.

10.20

Stock Option Agreement between Flanders Corporation and Robert R. Amerson dated February 22, 1996, filed with Form S-8 on July 21, 1997, incorporated herein by reference.

10.21

Amendment to Stock Option Agreement between Flanders Corporation and Robert R. Amerson dated December 22, 1999, filed with the Form 10-K dated December 31, 1999, and incorporated herein by reference.

10.22

Stock Option Agreement between Flanders Corporation and Robert R. Amerson dated November 7, 2001, filed with Form 10-K for December 31, 2001, incorporated herein by reference.

10.23

Stock Option Agreement between Flanders Corporation and Steven K. Clark dated February 22, 1996, filed with Form S-8 on July 21, 1997, incorporated herein by reference.

10.24

Amendment to Stock Option Agreement between Flanders Corporation and Steven K. Clark dated December 22, 1999, filed with the Form 10-K dated December 31, 1999, and incorporated herein by reference.

10.25

Stock Option Agreement between Flanders Corporation and Steven K. Clark dated November 7, 2001, filed with Form 10-K dated December 31, 2001, incorporated by reference.

10.26

Note Agreement between Steven K. Clark and Flanders Corporation, dated April 24, 1999, filed with the Form 10-K dated December 31, 1999, and incorporated herein by reference.

10.27

Note Agreement between Robert R. Amerson and Flanders Corporation, dated April 24, 1999, filed with the Form 10-K dated December 31, 1999, and incorporated herein by reference.

10.28

Stock Option Agreement between Flanders Corporation and Steven K. Clark dated August 24, 2004, filed with Form 10-K dated December 31, 2004, filed herewith.

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Subsidiaries of the Registrant.

23.1

Consent of Pender Newkirk LLP for incorporation by reference of their report into Form S-8 filed on July 21, 1997, filed herewith.

23.2

Consent of Grant Thornton LLP for incorporation by reference of their report into Form S-8 filed on July 21, 1997, filed herewith.

24

Power of Attorney (included on Signature page of this report).

32

Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of The Sarbanes-Oxley Act of 2002.

(b)

Form 8-K dated February 18, 2004

Form 8-K dated March 03, 2004

Form 8-K dated March 31, 2004

Form 8-K dated April 21, 2004

Form 8-K dated July 26, 2004

Form 8-K dated August 25, 2004

Form 8-K dated September 15, 2004

Form 8-K dated October 25, 2004

(c)

Financial Statement Schedules: See (a) (2) above.

SIGNATURES

Pursuant to the requirements of Section 13 of 15(d) 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.

Dated this 14th day of February, 2005.

FLANDERS CORPORATION

By /s/ Steven K. Clark

Steven K. Clark

President, Chief Executive Officer,

and Director

By /s/ John W. Hodson

John W. Hodson

Chief Financial Officer

KNOW ALL PERSONS BY THESE PRESENTS that each person whose signature appears below constitutes and appoints Steven K. Clark, his attorney-in-fact, to sign any amendments to this report, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Commission, hereby ratifying and confirming all the said attorney-in-fact may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Steven K. Clark	President, Chief Executive Officer And Director	
/s/ John W. Hodson	Chief Financial Officer	
/s/ William Mitchum, Jr.	Director	
/s/ Robert Kelly Barnhill, Sr.	Director	

/s/	Director
David M. Mock	

FLANDERS CORPORATION

CONSOLIDATED FINANCIAL STATEMENTS

Years Ended December 31, 2004, 2003 and 2002

Report of Independent Registered Public Accounting Firm

Board of Directors

Flanders Corporation and Subsidiaries

St. Petersburg, Florida

We have audited the accompanying consolidated balance sheets of Flanders Corporation and Subsidiaries (the Company) as of December 31, 2004 and December 31, 2003 and the related consolidated statements of operations, stockholders equity, and cash flows for the three years ended December 31, 2004. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and December 31, 2003 and the results of its operations and its cash flows for the three years in the period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America

We have also audited, in accordance with the standards of the Public Company Oversight Board (United States), the effectiveness of the Company s internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 14, 2005 expressed an unqualified opinion thereon.

Pender Newkirk & Company

Certified Public Accountants

Tampa, Florida

February 14, 2005

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-(f) promulgated under the Exchange Act as a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and effected by the Company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

•

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the Company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2004. In making this assessment, the Company's management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework.

Based on our assessment, management believes that, as of December 31, 2004, the Company's internal control over financial reporting is effective based on those criteria.

The Company's independent auditors have issued an audit report on our assessment of the Company's internal control over financial reporting.

Report of Independent Registered Public Accounting Firm

Board of Directors

Flanders Corporation and Subsidiaries

St. Petersburg, Florida

We have audited management s assessment, included in the accompanying Management s Annual Report on Internal Control Over Financial Reporting included in Item 9A, that Flanders Corporation and subsidiaries (the Company) maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). The Company s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management s assessment and an opinion on the effectiveness of the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management s assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management s assessment that the Company maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on the COSO criteria. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on the COSO criteria**.**

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets of the Company as of December 31, 2004 and 2003, and the related statements of operations, stockholders equity and cash flows for each of the three years in the period ended December 31, 2004 and our report dated February 14**,** 2005 expressed an unqualified opinion thereon.

Pender Newkirk & Company

Certified Public Accountants

Tampa, Florida

February 14, 2005

CONSOLIDATED BALANCE SHEETS

December 31,

(In thousands, except per share data)

ASSETS	**2004**	**2003**

Current assets		
	$	$
Cash and cash equivalents	1,886	1,098
Receivables:		
Trade, less allowance for doubtful accounts: $3,300 in 2004 and $2,949 in 2003	41,547	35,908
Other	240	265
Inventories	39,539	33,066
Deferred taxes	2,875	2,889
Other current assets	1,019	1,461
Total current assets	87,106	74,687
Related party receivables	374	362
Property and equipment, net	67,356	67,855
Intangible assets, net	888	880
Other assets	3,946	1,631
	$	$
	159,670	145,415
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities		
	$	$
Current maturities of long-term debt and capital lease obligations	2,553	2,542
Accounts payable	15,595	11,501
Accrued expenses	14,746	15,097
Total current liabilities	32,894	29,140
Long-term capital lease obligations, less current maturities	2,368	2,805
Long-term debt, less current maturities	18,138	20,943
Long-term liabilities, other	1,729	1,850
Deferred taxes	11,380	9,968
Commitments and contingencies		
Stockholders equity		
Preferred stock, $.001 par value, 10,000 shares authorized; none issued		
Common stock, $.001 par value; 50,000 shares authorized; issued and outstanding: 26,303	26	26
Additional paid-in capital	90,758	90,527
Notes receivable secured by common shares	(6,650)	(9,028)
Accumulated other comprehensive loss	(1,037)	(1,110)
Retained earnings	10,064	294
	93,161	80,709
	$	$
	159,670	145,415

CONSOLIDATED STATEMENTS OF OPERATIONS

Year Ended December 31,

(In thousands, except per share data)

		2004	2003	2002
		$	$	$
Net sales		199,933	182,780	184,211
Cost of goods sold		151,645	139,509	143,390
	Gross profit	48,288	43,271	40,821
Operating expenses		33,569	32,112	29,591
	Operating income	14,719	11,159	11,230
Non operating income (expense)				
Other income, net		1,209	1,970	1,272
Interest expense		(1,577)	(1,878)	(4,762)
		(368)	92	(3,490)
	Earnings from operations before income taxes	14,351	11,251	7,740
Provision for income taxes		4,581	3,505	3,001
	Earnings from operations	9,770	7,746	4,739
Cumulative effect of accounting change, net of tax				(27,681)
		$	$	$
	Net earnings (loss)	9,770	7,746	(22,942)
Earnings per share from operations				
		$	$	$
Basic		.37	0.30	0.18
		$	$	$
Diluted		.36	0.29	0.18

- Continued -

CONSOLIDATED STATEMENTS OF OPERATIONS Continued

Year Ended December 31,

(In thousands, except per share data)

	2004	2003	2002
Loss per share from cumulative effect of accounting change			
Basic	$	$	$ (1.06)
Diluted	$	$	$ (1.06)
Net earnings (loss) per share			
Basic	$ .37	$ 0.30	$ (0.88)
Diluted	$ .36	$ 0.29	$ (0.88)
Weighted average common shares outstanding			
Basic	26,201	26,033	26,033
Diluted	27,289	26,428	26,033

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

Years Ended December 31, 2004, 2003 and 2002

(In thousands)

Common Stock	Additional Paid-In Capital	Notes Receivable	Accumulated Other Comprehensive Loss	Retained Earnings	Total

Balance, January 1, 2002	26	90,331	(8,326)	(654)	15,502	96,879
Accrued interest on notes receivable secured by common shares			(369)			(369)
Comprehensive loss						
Net loss					(22,942)	(22,942)
Loss on cash flow hedges				(640)		(640)
Total comprehensive loss, net of tax						(23,582)
	$	$	$	$	$	$
Balance, December 31, 2002	26	90,331	(8,695)	(1,294)	(7,440)	72,928
Accrued interest on notes receivable secured by common shares			(333)			(333)
Purchase and retirement of 63 shares of common stock	(1)	(188)			(12)	(201)
Issuance of 106 shares of common stock upon exercise of options	1	384				385
Comprehensive loss						
Net earnings					7,746	7,746
Gain on cash flow hedges				184		184
Total comprehensive earnings, net of tax						7,930
	$	$	$	$	$	$
Balance, December 31, 2003	26	90,527	(9,028)	(1,110)	294	80,709
Accrued interest on notes receivable secured by common shares			(309)			(309)
Proceeds from notes receivable secured by common shares			2,687			2,687
Purchase and retirement of 19 shares of common stock		(88)				(88)
Issuance of 238 shares of common stock upon exercise of options		319				319
Comprehensive earnings						
Net earnings					9,770	9,770
Gain on cash flow hedges				73		73
Total Comprehensive earnings, net of tax						9,843
Balance, December 31, 2004	$	$	$	$	$	$
	26	90,758	(6,650)	(1,037)	10,064	93,161

CONSOLIDATED STATEMENTS OF CASH FLOWS

Year Ended December 31,

(In thousands)

	2004	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES			
	$	$	$
Earnings from continuing operations	9,770	7,746	4,739
Adjustments to reconcile earnings from continuing operations to net cash provided by operating activities:			
Depreciation and amortization	8,165	7,990	7,477
Provision for doubtful accounts and notes	2,039	3,466	1,048
Provision for obsolete inventory	69	208	425
Loss on sale of property and equipment	138	200	382
Gain on sale of assets			(286)
Deferred taxes	1,377	1,094	3,219
Accrued interest on notes receivable secured by common shares	(309)	(333)	(369)
Change in working capital components:			
Receivables	(10,882)	(4,882)	(4,894)
Inventories	(6,527)	(6,147)	3,274
Other current assets	181	(391)	893
Accounts payable	4,093	(2,296)	(1,929)
Accrued expenses	(350)	5,438	209
Income taxes (net)	386	220	2,436
Net cash provided by operating activities	8,150	12,313	16,624
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property and equipment	(7,563)	(5,264)	(3,636)
Proceeds from sale of property and equipment	172	142	1,656
Proceeds from sale of assets			1,498
Proceeds from (disbursements on) notes receivables	(13)	70	117
Decrease in other assets	267	42	449
Net cash provided by (used in) investing activities	(7,137)	(5,010)	84

- Continued -

CONSOLIDATED STATEMENTS OF CASH FLOWS Continued

Years Ended December 31,

(In thousands)

	2004	**2003**	**2002**
CASH FLOWS FROM FINANCING ACTIVITIES			
Net payments from revolving credit agreement	(654)	(6,799)	(20,525)
Proceeds from long-term borrowings			9,500
Principal payments on long-term borrowings	(2,576)	(2,528)	(5,727)
Payment of debt issuance costs	(1)	(51)	(1,028)
Proceeds from exercise of options	319	367	
Proceeds from notes receivable secured by common shares	2,687		
Net cash used in financing activities	(225)	(9,011)	(17,780)
Net increase (decrease) in cash and cash equivalents	788	(1,708)	(1,072)
CASH AND CASH EQUIVALENTS			
Beginning of year	1,098	2,806	3,878
End of year	$ 1,886	$ 1,098	$ 2,806
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION			
Interest paid, net of $39, $26 and $72 interest capitalized to property and equipment for 2004, 2003 and 2002, respectively:	$ 1,614	$ 1,954	$ 4,767
Income taxes paid/(received)	$ 4,044	$ 525	$ (2,654)
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES			
Cumulative effect of accounting change, net of taxes	$	$	$ (27,681)
Purchase and retirement of common stock	$ 88	$	$
Sale of assets in exchange for notes receivable	$	$ 2	$ 400
Capital lease obligation incurred for property and equipment	$	$ 143	$ 181

	$	$	$
Accounts receivable in exchange for notes receivable	3,395	149	

Note A.

Nature of Business and Summary of Significant Accounting Policies

The nature of the business and a summary of the significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements follows.

1.

Nature of business

The Company designs, manufactures and sells air filters and related products. It is focused on providing complete environmental filtration systems for end uses ranging from controlling contaminants in residences and commercial office buildings through specialized manufacturing environments for semiconductors and pharmaceuticals. The Company also designs and manufactures much of its own production equipment to automate processes to decrease labor costs associated with its standard products. The Company also produces glass-based air filter media for many of its products. The vast majority of the Company s current revenues come from the sale of after-market replacement filters, since air filters are typically placed in equipment designed to last much longer than the filters.

The Company sells some products for end users outside of the United States through domestic specialty clean room contractors. These sales are accounted for as domestic sales. The Company also sells products through foreign distributors, primarily in Europe, and through a wholly-owned subsidiary, which sells to customers in the Pacific Rim. Sales through foreign distributors and its wholly owned foreign subsidiary total less than 5% of net sales. Assets held outside the United States are negligible.

2.

Principles of consolidation

The consolidated financial statements include the accounts and operations of the Company and its subsidiaries, all of which are wholly-owned except for Superior Diecutting, Inc. of which 50% is owned by two officers and directors and 50% is owned by other shareholders unrelated to the Company or any of its officers and directors.

3.

Significant customers

Net sales for the years ended December 31, 2004, 2003 and 2002 included sales to the following major customers, together with the receivables due from those customers:

	Amount of Net Sales			Trade Receivable Balance	
				As of December 31,	
	2004	2003	2002	2004	2003
Customer A	$ 29,149	$ 30,715	$ 24,478	$ 5,132	$ 5,507
Customer B	$ 31,581	$ 30,770	$ 27,579	$ 9,320	$ 6,302

4.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note A.

Nature of Business and Summary of Significant Accounting Policies Continued

5.

Cash and cash equivalents

The Company maintains its cash in bank deposit accounts, which at times, exceed federally insured limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents. For purposes of reporting cash flows, the Company considers all cash accounts which are not subject to withdrawal restrictions or designated for equipment acquisitions and certificates of deposit which have an original maturity of three months or less when purchased to be cash equivalents.

6.

Accounts Receivable

The Company provides an allowance for losses on trade receivables based on a review of the current status of existing receivables and management s evaluation of periodic aging of accounts. The Company charges off accounts receivable against the allowance for losses when an account is deemed to be uncollectible. It is the Company s policy to accrue interest on past due receivables. The provision for doubtful accounts and notes was $2,039, $3,466, and $1,048 for the years ended December 31, 2004, 2003 and 2002, respectively.

7.

Fair value of financial instruments

The carrying amount of cash equivalents, trade receivables and trade payables approximates fair value at December 31, 2004 and 2003 because of the short maturity of these instruments. Based on the borrowing rates currently available to the Company for bank loans with similar maturities and similar collateral requirements, the fair value of notes payable and long-term debt approximates the carrying amounts at December 31, 2004 and 2003.

8.

Inventories

Inventories are valued at lower of cost (first-in, first-out method) or market.

9.

Comprehensive income

FAS 130, Reporting Comprehensive Income, requires disclosure of comprehensive income in addition to the existing income statement. Other comprehensive income (loss) is defined as the change in equity during a period, from transactions and other events, excluding changes resulting from investments by owners (e.g., supplemental stock offerings) and distributions to owners (e.g., dividends). An analysis of the changes in the components of accumulated comprehensive income is presented in the statement of changes in stockholders equity.

10.

Derivative financial instruments

Effective January 1, 2001, the Company adopted Statement of Financial Accounting Standard No. 133, Accounting for Derivative Instruments and Hedging Activities (SFAS 133) as amended by SFAS 138, Accounting for Certain Derivative Instruments and Hedging Activities -- an Amendment to FASB Statement No. 133. SFAS 133 and SFAS 138 established new accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. All derivatives, whether designated in hedging relationships or not, are required to be recorded on the balance sheet at fair value. If the derivative is a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in other comprehensive income and are recognized in the income statement when the hedged item affects earnings. Ineffective portions of changes in the fair value of cash flow hedges are recognized in earnings

Note A.

Nature of Business and Summary of Significant Accounting Policies Continued

The Company has only limited involvement with derivative financial instruments. The Company has two interest rate swap agreements to hedge against the potential impact on earnings from increases in market interest rates of two variable rate bonds. Under the interest rate swap agreements, the Company receives or makes payments on a monthly basis, based on the differential between 5.14% and a tax exempt interest rate as determined by a remarketing agent. This interest rate swap is accounted for as a cash flow hedge in accordance with SFAS 133 and SFAS 138. The tax effected fair market value of the interest rate swap of $1,037 and $1,110 is included in accumulated other comprehensive loss at December 31, 2004 and 2003, respectively. The interest rate swap contracts expire in 2013 and 2015.

11.

Goodwill

As of January 1, 2002, the Company adopted Statement of Financial Accounting Standard (SFAS) No. 142,   Goodwill and Other Intangible Assets   (SFAS 142). SFAS 142 changes the accounting for goodwill from an amortization method to an impairment-only approach. Thus, effective January 1, 2002, the Company has ceased amortization of goodwill, including goodwill recorded in past business combinations. The Company does not have any intangible assets with indefinite lives other than goodwill.

SFAS 142 requires that goodwill be tested for impairment annually, or more frequently if circumstances indicate potential impairment, by comparing the fair value of the asset to its carrying amount. Such testing requires, as an initial step, that each of the Company s reporting units, as defined in SFAS 142, be identified and that the Company s assets and liabilities, including the existing goodwill and intangible assets, be assigned to those reporting units. The Company has determined it has only one reporting unit.

During the fourth quarter of 2002, the Company completed its transitional impairment analysis. An independent third party performed valuations of the Company. The third party performing the valuation concluded, based on various methodologies, that the fair value of the Company exceeded its carrying value, and thus, there was no goodwill impairment. In addition, the Company s independent certifying accountants, in accordance with SAS 73 (Using the Work of a Specialist), evaluated the professional qualifications of the third party evaluator, gained an understanding of the work performed, which included an understanding of the specialist s work, methods, and assumptions used and made appropriate tests of data provided to the specialists. The independent certifying accountants concluded that the specialist s findings were supported by the data provided. However, according to SFAS 142, quoted market prices in active markets are the best evidence of fair value, and thus the Company, with the concurrence of the Company s independent certifying accountants, concluded that the higher fair value, as determined by the third party valuation, is not sufficient to outweigh the presumption of fair value indicated by the quoted market price of the Company. Accordingly, the Company determined that an impairment charge upon the adoption of SFAS 142 on January 1, 2002 was necessary.

12.

Trademarks and trade names

Trademarks and trade names are being amortized on a straight line basis over 17 years. At each balance sheet date, the Company evaluates the value of trademarks and trade names for impairment. Based upon its most recent analysis, the Company believes that no impairment of trademarks and trade names exists at December 31, 2004.

Note A.

Nature of Business and Summary of Significant Accounting Policies Continued

13.

Property and equipment

Property and equipment are stated at cost. Depreciation is computed by the straight-line method over estimated useful lives. Amortization of property and equipment held under capital leases is included in depreciation expense. The carrying amount of all long-lived assets is evaluated periodically to determine if adjustment to the depreciation and amortization period or the unamortized balance is warranted. Based upon its most recent analysis, the Company believes that no impairment of property and equipment exists at December 31, 2004.

14.

Debt issuance costs

The costs related to the issuance of debt are capitalized and amortized on a straight-line basis over the term of the related debt, which approximates the effective interest method.

15.

Revenue recognition

Generally, sales are recognized when shipments are made to customers. Rebates, allowances for damaged goods and other advertising and marketing program rebates, are accrued pursuant to contractual provisions and included in accrued expenses. An insignificant amount of our revenues fall under the percentage-of-completion method of accounting used for long-term contracts. Under this method, sales and gross profit are recognized as work is performed based on the relationship between actual costs incurred and total estimated costs at completion. Sales and gross profit are adjusted prospectively for revisions in estimated total contract costs and contract values. Estimated

losses are recorded when identified.

16.

Income taxes

Deferred taxes are provided on the liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carry forwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

17.

Earnings (loss) per share

Basic EPS is calculated by dividing earnings (loss) available to common shareholders by the weighted average number of common shares outstanding during each period. Diluted EPS is similarly calculated, except that the denominator includes common shares that may be issued subject to existing rights with dilutive potential, except when their inclusion would be antidilutive.

Note A.

Nature of Business and Summary of Significant Accounting Policies Continued

18.

Stock Options

At December 31, 2004, the Company has three stock-based compensation plans. The Company accounts for those plans under the recognition and measurement principles of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees and related Interpretations. No stock-based compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement 123, Accounting for Stock-Based Compensation , to stock-based employee compensation.

	2004	2003	2002
Net earnings (loss), as reported	$ 9,770	$ 7,746	$ (22,942)
Deduct: Total stock-based compensation expense determined under fair value based methods for all awards, net of taxes	(2,454)	(562)	(149)
Pro forma net earnings (loss)	$ 7,316	$ 7,184	$ (23,091)
Basic earnings (loss) per share:			
As reported	$ .37	$ .30	$ (.88)
Pro forma	$ .28	$ .28	$ (.89)
Diluted earnings (loss) per share			
As reported	$ .36	$ .29	$ (.88)
Pro forma	$ .27	$ .27	$ (.89)

19.

Outbound shipping expenses

Outbound shipping expenses are included in operating expenses, not in cost of goods sold. Outbound shipping expenses were $8,224, $6,724, and $6,186 for the years ending December 31, 2004, 2003 and 2002, respectively.

20.

Advertising

The costs of advertising are expensed as incurred. Advertising expense was $2,422, $2,001, and $1,672 for the years ending December 31, 2004, 2003 and 2002, respectively.

21.

Reclassifications

Certain account balances for 2003 and 2002 have been reclassified with no effect on net earnings or retained earnings to be consistent with the classification adopted for the year ended December 31, 2004.

Note A.

Nature of Business and Summary of Significant Accounting Policies   Continued

22.

Impact of Recently Issued Accounting Pronouncements

In June 2002, the Financial Accounting Standards Board issued SFAS 146,   Accounting for Costs Associated with Exit or Disposal Activities . SFAS 146 provides direction for accounting and disclosure regarding specific costs related to an exit or disposal activity. These include, but are not limited to, costs to terminate a contract that is not a capital lease, costs to consolidate facilities or relocate employees, and certain termination benefits provided to employees that are involuntarily terminated under the terms of a one-time benefit arrangement. The Company is required to adopt SFAS 146 for any disposal activities initiated after December 31, 2002. Management does not expect the adoption of SFAS 146 to have a material impact on the Company s financial statements and results of operations.

In December 2002, the Financial Accounting Standards Board issued SFAS 148,   Accounting for Stock Based Compensation Transition and Disclosure an Amendment of SFAS 123   (SFAS 148). SFAS 148 provides additional transition guidance for those entities that elect to voluntarily adopt the provisions of SFAS 123. Furthermore, SFAS 148 mandates new disclosures in both interim and year-end financial statements within the Company s Significant Accounting Policies footnote. The Company is currently reviewing the impact of SFAS 148 on its financial statements. Management does not expect the adoption of SFAS 148 to have a material impact on the Company s financial statements and results of operations.

In January 2003, the Financial Accounting Standards Board (FASB) issued Interpretation No. 46,   Consolidation of Variable Interest Entities, an Interpretation of Accounting Research Bulletin No. 51   (the   Interpretation). The Interpretation requires the consolidation of variable interest entities in which an enterprise absorbs a majority of the

entity s expected losses, receives a majority of the entity s expected residual returns, or both, as a result of ownership, contractual, or other financial interests in the entity. Currently, entities are generally consolidated by an enterprise that has controlling financial interest through ownership of a majority voting interest in the entity. The Interpretation was originally immediately effective for variable interest entities created after January 31, 2003, and effective in the fourth quarter of the Company s fiscal 2003 for those created prior to February 1, 2003. However, in October 2003, the FASB deferred the effective date for those variable interest entities created prior to February 1, 2003, until the Company s first quarter of fiscal 2004. The Company has substantially completed the process of evaluating this interpretation and believes its adoption will not have a material impact on its consolidated financial statements.

In May 2003, the FASB issued SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity. This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement is effective for financial instruments entered into or modified after May 31, 2003 and pre-existing instruments as of the beginning of the first interim period that commences after June 15, 2003, except for mandatorily redeemable financial instruments. Mandatorily redeemable financial instruments are subject to the provisions of this statement beginning on January 1, 2004. We have not entered into or modified any financial instuments subsequent to May 31, 2003 affected by this statement. We do not expect the adoption of this statement will have a material impact on our financial condition or results of operations.

In November 2004, the Financial Accounting Standards Board issued statement of Financial Accounting Standard No. 151, "Inventory Costs". The new Statement amends Accounting Research Bulletin No. 43, Chapter 4, "Inventory Pricing," to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. This Statement requires that those items be recognized as current-period charges and requires that allocation of fixed production overheads to the cost of conversion be based on the normal capacity of the production facilities. This statement is effective for fiscal years beginning after June 15, 2005. We do not expect adoption of this statement to have a material impact on our financial condition or results of operations.

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment. This Statement replaces FASB Statement No. 123 and supersedes APB Opinion No. 25. Statement No. 123(R) will require the fair value of all stock option awards issued to employees to be recorded as an expense over the related vesting period. The Statement also requires the recognition of compensation expense for the fair value of any unvested stock option awards outstanding at the date of adoption. We are evaluating these new rules, but expect no material impact upon adoption relating to outstanding options since a majority of the awards under the existing incentive stock option plan will be fully vested prior to the effective date of the revised rules.

Note B. Inventories

Inventories consist of the following at December 31:

	2004	2003
	$	$
Finished goods	19,233	14,625
Work in progress	2,630	3,403
Raw materials	19,068	16,361
	40,931	34,389
Less allowances	1,392	1,323
	$ 39,539	$ 33,066

Note C. Other Assets

Other assets consist of the following at December 31:

	2004	2003
	$	$
Real estate held for sale	52	52
Notes receivable	2,607	478
Deposits	238	238
Deferred expenses	649	863
Investment, at cost	400	
	$ 3,946	$ 1,631

Notes receivable consists of the following at December 31,

	2004	2003
Note receivable, which is interest free for first year and 9% per annum thereafter, with a second year interest free if $450 is paid during the first year. $4 due each week beginning July1, 2004.	$ 912	$ 0
Senior note receivable, which is interest free for first year and 5% per annum thereafter. $6.5 due each month beginning January 31, 2005.	500	0
Junior note receivable, which is interest free. $5 due each quarter beginning March 31, 2005.	300	0
Note receivable due in full by June 30, 2011.	1,000	0
Various other notes receivable	360	818
Less: Current portion of notes receivable	(465)	(340)
Total	$ 2,607	$ 478

Note D. Intangible Assets

Intangible assets consist of the following at December 31:

	2004	2003
Trademarks and trade names, net of accumulated amortization of $820 and $641 in 2004 and 2003, respectively	$ 888	$ 880
	$ 888	$ 880

Amortization expense was $179, $133 and $60 in 2004, 2003 and 2002, respectively. Estimated amortization expense for each of the ensuing years through December 31, 2009 is as follows:

2005	$ 194
2006	$ 98
2007	$ 98
2008	$ 98
2009	$ 73

Note E. Property and Equipment

Property and equipment and estimated useful lives consist of the following at December 31:

Estimated

	2004	2003	Useful Lives
	$	$	
Land	1,635	1,389	
Buildings	40,153	39,105	15-40 years
Machinery and equipment	66,404	59,059	5 -15 years
Office equipment	9,866	9,658	5-7 years
Vehicles	1,351	1,171	5 years
Construction in progress	2,914	4,887	
	122,323	115,269	
Less accumulated depreciation	54,967	47,414	
	$ 67,356	$ 67,855	

Total depreciation expense charged to operations totaled $7,771, $7,614, and $7,376 for 2004, 2003 and 2002, respectively.

Note F. Accrued Expenses

Accrued expenses at December 31, 2004 and 2003 were as follows:

	2004	2003
Income tax payable	$ 975	$ 1,958
Bank overdraft	2,631	4,738
Other accrued expenses	11,140	8,401
	$ 14,746	$ 15,097

Note G. Pledged Assets and Debt

A summary of the Company s debt, and collateral pledged thereon, consists of the following at December 31:

	2004	2003
Long-term debt:		

LIBOR (3.1% at December 31, 2004) plus 1.75 to 2.25% revolving line of credit; interest rate dependent on fixed charge coverage*.	$ 0	$ 654
LIBOR plus 2.5 to 3.0% term note agreement; interest rate dependent on fixed charge coverage*.	3,967	5,367
LIBOR plus 2.25% note (mortgage) payable to a bank, due in monthly payments of $14 including interest through October 2007, at which time all unpaid principal is due, collateralized by certain land, building and improvements.	2,118	2,292
Prime plus 0.25 percent (5.25% at December 31, 2004) notes payable to a mortgage company due in monthly payments of $30 including interest through January 2006, at which time all unpaid principal is due, collateralized by a deed of trust on land and buildings.	303	570
6.5 percent note payable to a regional development authority, due in varying quarterly installments, plus interest, through December 2017, collateralized by a security agreement and financing statement on real and personal property.	4,685	4,910
Note payable to a bank with interest at prime plus 0.25 percent, with rate adjusted annually (5.25% at December 31, 2004), due in monthly payments of $7 including interest through June 2017 subject to a call option in June 2007, collateralized by a deed of trust on real property.	684	724
Industrial revenue bond with a variable tax exempt interest rate as determined by a remarketing agent, with rate effectively fixed at 5.14% by an interest-rate swap, collateralized by a $4,000 letter of credit that expires April 1, 2015.	4,000	4,000
Industrial revenue bond with a variable tax exempt interest rate as determined by a remarketing agent, with rate effectively fixed at 5.14% by an interest-rate swap, collateralized by a $4,500 letter of credit that expires April 1, 2013.	4,500	4,500
Various obligations under capital lease agreements	2,802	3,273
	$ 23,059	$ 26,290

Note G.

Pledged Assets and Debts Continued

Less current maturities	2,553	2,542
	20,506	23,748
Less long-term capital lease obligations, less current maturities	2,368	2,805
	$ 18,138	$ 20,943

Aggregate maturities required on long-term debt and capital lease obligations as of December 31, 2004 are due in future years as follows:

Year Ending December 31,

	$
2005	2,553
2006	2,361
2007	3,773
2008	876
2009	948
Later years	12,548
	$ 23,059

*

Our current revolving credit agreement with a bank provides a maximum line of credit of $33 million (subject to availability) and bears interest at either (i) LIBOR plus between 1.75% and 2.25%, dependent on the Company s fixed charge coverage during the prior twelve months; or (ii) the greater of the Federal Funds Effective Rate plus 0.5% or the bank s base rate, plus between 0.5% and 1%, dependent on the Company s fixed charge coverage during the prior twelve months. Up to $11 million of this credit facility may be used to issue letters of credit of which the Company has two letters of credit associated with its industrial revenue bonds and two associated with its workers compensation policy. The revolving credit agreement is part of a combined facility with a bank that also includes a $7 million facility to guarantee letters of credit, and a term loan at an interest rate 0.75% higher than the revolving facility. The term loan is due in monthly principal payments of $116 plus interest. Both the line of credit and term loan are due in 2007. The combined facility is collateralized by substantially all of the Company s assets, requires maintenance of certain financial ratios, and restricts capital expenditures, payment of dividends and share repurchases.

Note H.

Leases

The Company leases certain facilities and equipment under long-term non-cancelable operating leases, which may be renewed in the ordinary course of business, including a building lease with a related party. The Company leases certain manufacturing and warehousing space under a capital lease with an original term of ten years with two consecutive ten-year renewal options. Leased capital assets are included in property and equipment as follows at December 31:

	2004	**2003**
	$	$
Buildings	3,700	3,700
Machinery and equipment	439	439
Office equipment	358	358
Accumulated depreciation	(907)	(676)
	$	$
	3,590	3,821

Future minimum payments, by year and in aggregate, under capital leases and operating leases consist of the following at December 31, 2004:

Year Ending December 31,

	Capital leases	Operating leases
	$	$
2005	666	2,253
2006	658	1,034
2007	654	491
2008	640	145

2009	641	125
Later years	272	125
Total minimum lease payments	$ 3,531	$ 4,173
Less amount representing interest	729	
Present value of net minimum payments	2,802	
Current portion	434	
Long-term portion	$ 2,368	

Total rent expense charged to operations was approximately $3,360, $3,255, and $2,946 for 2004, 2003 and 2002, respectively.

Note I.

Income Taxes

The Company s provision (benefit) for income taxes is as follows for the years ended December 31:

	2004	2003	2002
Current:			
Federal	$ 3,449	$ 2,164	$ (319)
State	296	185	(43)
Foreign	150	62	144
	3,895	2,411	(218)
Deferred:			
Federal	632	1,008	2,843
State	54	86	376
	686	1,094	3,219
Total provision	$ 4,581	$ 3,505	$ 3,001

The income tax provision for continuing operations differs from the amount of tax determined by applying the Federal statutory rate as follows:

		2004	2003	2002
		$	$	$
Income tax provision at statutory rate:		5,068	3,938	2,632
Increase (decrease) in income taxes due to:				
	Nondeductible expenses	19	22	35
	State income taxes net	561	334	334
	Credits and adjustments	(1,067)	(789)	
		$	$	$
		4,581	3,505	3,001

Continued

Net deferred tax assets and liabilities were comprised of the following:

		2004	2003
Deferred tax assets:			
		$	$
	Accounts receivable allowance	870	642
	Inventory allowance and capitalization	1,177	905
	Accrued expenses	579	541
	Deferred expenses	40	41
	Other Reserves		260
	State credits	209	500
		$	$
		2,875	2,889
Deferred tax liabilities:			
		$	$
	Property and equipment	(13,592)	(10,913)

Interest rate swap	692	740
State net operating loss carry forwards	222	205
State credits	1,298	0
	$ (11,380)	$ (9,968)

The components giving rise to the net deferred tax assets and liabilities described above have been included in the accompanying consolidated balance sheets at December 31 as:

	2004	2003
	$	$
Current assets	2,875	2,889
Noncurrent liabilities	(11,380)	(9,968)
	$ (8,505)	$ (7,079)

Note J.

Commitments and Contingencies

1.

Employment Agreements

Messrs. Amerson and Clark have employment agreements effective as of December 15, 1995 (Employment Agreements). The Employment Agreements, as amended, provide for an annual base salary of $250 for both Mr. Amerson and Mr. Clark and terminate in 2010. The Employment Agreements also provide that the executive shall be entitled to the following termination payments: (i) 100% of his current base salary if the employment is terminated as a result of his death or disability; (ii) up to 200% of his current base salary if the employment is terminated by the Company for any reason other than death, disability or for cause, or (iii) up to 250% of the executive s gross income during the year preceding his termination if the Employment Agreement is terminated by the executive for good reason or by the Company for any reason other than death, disability or cause and the termination occurs within two years after a change of control of the Company has occurred.

Messr. Hodson has a two year employment contract dated January 1, 2005. The employment contract for Hodson provides for an annual base salary of 100K and a discretionary bonus. The Employment Agreement also provides for 200% of his base salary upon termination by the company for any reason other than death or disability.

Continued

2.

Litigation

The Company is involved in a dispute with Liberty Mutual, a former workers compensation administrator and stop-loss insurer for some of the Company s subsidiaries. The administrator has alleged that they are entitled to be reimbursed for certain costs incurred in administering various insurance claims. The Company has counter-sued, claiming that the administrator acted in bad faith, was negligent in its duties as administrator of our claims, that it made payments on our behalf which were specifically disallowed, that they refused to follow instructions given to them by us, that they failed to meet minimal acceptable standards for administering claims, and that such failures constituted a material dereliction of their responsibilities as administrator, as well as other claims related to malfeasance and negligence. In addition, Liberty Mutual charged certain administrative fees over and above the actual costs incurred which the Company is contesting. The amount and probability of any payment or settlement is unknown at this time. Among the issues being considered is the ripeness of our counterclaim as well as the matter of currently unresolved workers compensation claims whose estimate of potential loss may change as a result of this litigation. While management believes it has reserved an adequate amount for settlement of these claims, there is no guarantee that the Company s actual liability will not exceed its current estimate. Accordingly, these matters, if resolved in a manner different from management s estimate, could have a material effect on operating results or cash flows in the future.

We have settled our lawsuit with Conap (U.S. District Court for the Eastern District of North Carolina, Case No. 4-99-CV-93-H(3)) a supplier of urethane sealant used in some of our HEPA filtration products. The settlement amount we received is included in other income.

From time to time, the Company is a party as plaintiff or defendant to various legal proceedings related to our normal business operations. In the opinion of management, although the outcome of any legal proceeding cannot be predicted with certainty, the ultimate liability of the Company in connection with its legal proceedings will not have a material

adverse effect on the Company s financial position, but could be material to the results of operations in any one future accounting period. The Company makes appropriate reserves for litigation, even if not material. Defense costs are expensed as incurred.

3.

Self-Insurance

During all periods presented, workers compensation claims incurred by employees were fully insured through a high deductible policy with a policy year ending each May. The deductible per employee was $350 for 2004 and 2003, with no limit in the aggregate. The Company continuously monitors and estimates the estimated costs of claims incurred based on historical loss information and other information provided by its carrier s claims management personnel. Included in the liabilities in the accompanying balance sheets are accrued workers compensation expenses of approximately $659 and $646 as of December 31, 2004 and 2003, respectively.

The Company provides medical benefits to its employees under a self-insured program. Through June 30, 2002, the Company paid for 100% of an employees health costs as the services were incurred. In July 2002, the Company changed the program that provides medical benefits to its employees once certain deductibles are met. The benefits to the employees are limited to $35 per year with a $1,000 lifetime benefit. The Company estimates the amount of incurred but unreported claims based on historical information. Included in the liabilities in the accompanying balance sheets are estimated accrued health insurance expenses of approximately $232 and $228 as of December 31, 2004 and 2003, respectively. The employer s portion of claims charged to operations totaled approximately $893, $919 and $2,297 for 2004, 2003 and 2002, respectively.

4.

License and Royalty Agreements

The Company has secured licensing and royalty agreements with two companies allowing the Company to use their trade names and brands on its products. Costs associated with these agreements are expensed as incurred.

Note K.

Employee Benefit Plans

The Company has a defined contribution 401(k) salary reduction plan intended to qualify under section 401(a) of the Internal Revenue Code of 1986 (Salary Savings Plan). The Salary Savings Plan allows eligible employees, as defined in the plan document, to defer up to fifteen percent of their eligible compensation, with the Company contributing an amount determined at the discretion of the Company s Board of Directors. The Company contributed approximately $90, $89 and $102 to the Salary Savings Plan for the years ended December 31, 2004, 2003 and 2002, respectively.

During 1996, the Company adopted the Long Term Incentive Plan (LTI Plan) to assist the Company in securing and retaining key employees and consultants. The LTI Plan authorizes grants of incentive stock options, nonqualified stock options, stock appreciation rights (SARs), restricted stock performance shares and dividend equivalents to officers, key employees of the Company and outside consultants to the Company. There are 1,987,000 shares of Common Stock reserved for award under the LTI Plan. During 2004, 2003 and 2002, the Company awarded options to purchase 645,000, 145,000 and 85,000 shares of Common Stock under the LTI Plan, respectively.

During 1996, the Company also adopted the 1996 Director Option Plan which provides for the grant of 50,000 stock options to outside directors of the Company who were elected or appointed after February 1, 1996, and who were not existing directors on the effective date of the plan. Each such outside director who is serving as a director on January 1 of each calendar year will automatically be granted an option to acquire up to 5,000 shares of Common Stock on such date, assuming such outside director had been serving for at least six months prior to the date of grant. The Company has reserved 500,000 shares of its Common Stock for issuance under the 1996 Director Option Plan that expires in 2006. During 2004, 2003 and 2002, the Company awarded options to purchase 15,000, 80,000 and 155,000 shares, respectively, of Common Stock under the 1996 Director Option Plan.

Note L.

Related Party Transactions and Balances

At December 31, 2004 and 2003, the Company had notes receivable secured by common stock classified as contra-equity of $6,650 and $9,028, respectively, due from various directors, officers, shareholders and employees, with interest thereon at LIBOR plus 1%, maturing at various dates to December 2010, of which $6,650 is callable on demand by the Company if the officers or employees terminate employment with the Company.

During November 2000, the Company entered into a five-year operating lease whereby the Company was leasing 138,000 square feet of building owned by two officers of and directors of the Company (fifty percent each). In September 2002, the lease was amended as the Company occupied 224,000 square feet of building. Then, by November 2002, the Company occupied 399,000 square feet of a building. The Company made payments of $1,041, $1,030 and $474 in 2004, 2003 and 2002, respectively. The Company believes this lease is at prevailing market rates.

On January 2, 2001, the Company purchased and leased back $797 in manufacturing equipment from Superior Diecutting, Inc., a vendor 50% owned by two officer and directors. The Company also loaned this supplier $500,

secured by a building and used to pay off an existing mortgage, and $400 to repay a credit line secured by inventory, receivables and other current assets. The Company made payments of $6,933, $3,738 and $1,666 in 2004, 2003 and 2002, respectively, to this supplier for purchases of raw materials. At December 31, 2004 and 2003, the Company owed a total of $2,591 and $892, respectively, to this vendor. At December 31, 2004, Superior Diecutting, Inc. owed the Company $5,881 due to the Company purchasing inventory on behalf of Superior Diecutting, Inc. The accounts and operations of this related entity have been consolidated, thus, the financial effects of these transactions have been eliminated in consolidation.

Note M.

Stock Options and Warrants

During 2004, the Company granted options to purchase: 645,000 shares of common stock under its LTI Plan at exercise prices between $5.21 - $8.60 per share; 15,000 shares of common stock under its 1996 Director Option Plan at a weighted average exercise price of $4.92 per share. All options granted during 2004 were non-qualified fixed price options.

The following table summarizes the activity related to all Company stock options and warrants for 2004, 2003 and 2002:

	Shares (In thousands)		Exercise Price per Share				Weighted Average Exercise Price per Share	
	Warrants	Stock Options	Warrants		Options		Warrants	Options
Outstanding at January 1, 2002	540	4,698	8.40	14.73	1.88	8.50	10.04	4.89
Granted		240			1.50	2.36		1.69
Exercised								
Canceled or expired	(540)	(339)	8.40	14.73	1.88	8.50	10.04	4.26
Outstanding at December 31, 2002		4,599			1.50	7.50		4.76
Granted		225			1.65	5.00		3.51
Exercised		(106)			1.65	3.94		3.45
Canceled or expired		(183)			1.50	5.38		4.44
Outstanding at December 31, 2003		4,535			1.50	7.50		4.75
Granted		660			5.21	8.60		8.14
Exercised		(177)			1.65	6.49		2.18
Canceled or expired		(3)			4.75	4.75		4.75
Outstanding at December 31, 2004		5,015			1.50	8.60		5.28

Exercisable at December 31, 2004	4,835	1.74	8.60	5.36
Exercisable at December 31, 2003	4,350	1.65	7.50	4.95
Exercisable at December 31, 2002	4,464	1.74	7.50	4.86

The warrants and options expire at various dates ranging from February 2006 to August 2009. A further summary of information related to options outstanding at December 31, 2004 is as follows:

Range of Exercise Prices	Number Outstanding / Exercisable	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price Outstanding / Exercisable
$1.50 to 2.40	90 / 50	2.42	$1.72 / 1.90
$2.50 to 4.37	2,215 / 2,135	1.35	$2.58 / 2.58
$5.00 to 6.49	150 / 90	4.02	$5.17 / 5.28
$7.50 to 8.60	2,560 / 2,560	2.46	$7.74 / 7.74

As permitted under accounting principles generally accepted in the United States of America, grants to employees under the LTI Plan and other grants to employees of options are accounted for following APB Opinion No. 25 and related Interpretations. Accordingly, no compensation cost has been recognized for grants to employees under the LTI Plan, since all options granted had an exercise price at or above the quoted market price of the Company s common stock on the date of grant.

Continued

Had compensation cost for the option plans been determined based on the grant date fair values of awards using the Black-Scholes option pricing model, reported net earnings (loss) and earnings (loss) per common share would have been changed to the pro forma amounts shown below for the years ended December 31:

	2004	**2003**	**2002**
Net earnings (loss):			
As reported	$ 9,770	$ 7,746	$ (22,942)
Pro forma	$ 7,316	$ 7,185	$ (23,091)
Basic earnings (loss) per share:			
As reported	$	$	$

	$ .37	$ 0.30	$ (0.88)
Pro forma	$ .28	$ 0.28	$ (0.89)
Diluted earnings (loss) per share:			
As reported	$ .36	$ 0.29	$ (0.88)
Pro forma	$ .27	$ 0.27	$ (0.89)
Weighted average fair value per option of options			
Granted during the year	$ 6.21	$ 2.50	$ 1.04

In determining the pro forma amounts above, the value of each grant is estimated at the grant date using the Black-Scholes option model with the following weighted average assumptions for options granted in 2004, 2003 and 2002: Dividend rate of 0%; risk-free interest rate of 3.63%, 3.38% and 3.00%, respectively; expected lives of 5 years; and expected price volatility of 102%, 92% and 88%, respectively.

Note N.

Earnings (Loss) per Share

The following data show the shares used in computing net earnings (loss) per common share including dilutive potential common stock.

	2004	2003	2002
Common shares outstanding at beginning of year	26,084	26,033	26,033
Net weighted average common shares issued and canceled during year	117		
Weighted average number of common shares used in basic EPS	26,201	26,033	26,033
Dilutive effect of stock options and warrants	1,089	395	
Weighted average number of common shares and dilutive potential shares used in diluted EPS	27,290	26,428	26,033

As of December 31, 2004, 2003 and 2002, options and warrants to purchase 0, 2,000 and 4,539 shares, respectively, of the Company s common stock described in Note N were excluded from the computation of diluted EPS because the market price of the underlying stock was less than the exercise price.

Note O.

Quarterly Financial Data (Unaudited)

	Quarters Ended			
	March 31, 2004	June 30, 2004	September 30, 2004	December 31, 2004
Net sales	$ 45,354	$ 47,138	$ 54,785	$ 52,656
Gross profit	$ 9,963	$ 11,911	$ 12,646	$ 13,768
Operating income	$ 2,021	$ 3,486	$ 3,980	$ 5,232
Net Earnings	$ 1,454	$ 2,097	$ 2,784	$ 3,435
Net Earnings per share:	$	$	$	$
Basic	.06	.08	.11	.13
Diluted	.05	.08	.10	.13
Common stock prices:				
High	$ 7.26	$ 9.99	$ 10.47	$ 10.17
Low	5.21	6.12	8.36	8.17
	March 31, 2003	June 30, 2003	September 30, 2003	December 31, 2003
Net sales	$ 43,049	$ 44,262	$ 50,189	$ 45,280
Gross profit	$ 9,460	$ 10,838	$ 11,887	$ 11,086
Operating income	$ 2,111	$ 2,615	$ 3,576	$ 2,857
Net Earnings	$ 1,644	$ 2,260	$ 2,315	$ 1,527
Net Earnings per share:	$	$	$	$
Basic	.06	.09	.09	.06
Diluted	.06	.08	.09	.06
Common stock prices:				
High	$	$	$	$

	2.23	2.95	6.05	7.01
Low	1.43	2.09	2.71	4.45

FLANDERS CORPORATION

FINANCIAL STATEMENT SCHEDULE

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

ON SCHEDULE

Board of Directors and Stockholders

Flanders Corporation

In connection with our audits of the consolidated financial statements of Flanders Corporation and Subsidiaries referred to in our report dated February 14, 2005, which is included in the Company s Annual Report of Form 10-K for the year ended December 31, 2004, we have also audited Schedule II for each of the three years in the period ended December 31, 2004. In our opinion, this schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ Pender Newkirk & Company

Tampa, Florida

February 14, 2005

FLANDERS CORPORATION AND SUBSIDIARIES

SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS

Years Ended December 31, 2004, 2003 and 2002

	Balance at Beginning of Period	Additions Charged to Cost and Expense	Deductions	Balance at End of Period
For the year ended December 31, 2004				
	$	$	$	$
Allowance for doubtful accounts	2,949	1,875	(1,524)(1)	3,300
Allowance for inventory	1,323	69		1,392
	$	$	$	$
Total	4,272	1,944	(1,524)	4,692
For the year ended December 31, 2003				
	$	$	$	$
Allowance for doubtful accounts	2,240	3,151	(2,442)(1)	2,949
Allowance for inventory	1,115	208		1,323
	$	$	$	$
Total	3,355	3,359	(2,442)	4,272
For the year ended December 31, 2002				
	$	$	$	$
Allowance for doubtful accounts	1,532	1,048	(340)(1)	2,240
Allowance for inventory	1,149	425	(459)(2)	1,115
	$	$	$	$
Total	2,681	1,473	(799)	3,355

(1)

Uncollected receivables written-off, net of recoveries.

(2)

Reduction in allowance, offset to inventory.