

Edgar Filing: AAON INC - Form 10-Q

AAON INC  
Form 10-Q  
May 08, 2008

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2008  
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: 0-18953

AAON, INC.

(Exact name of registrant as specified in its charter)

Nevada

87-0448736

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(State or other jurisdiction  
of incorporation or organization)

(IRS Employer  
Identification No.)

2425 South Yukon, Tulsa, Oklahoma 74107

-----  
(Address of principal executive offices)  
(Zip Code)

(918) 583-2266

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(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

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

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

Yes  No

As of March 31, 2008 registrant had outstanding a total of 17,976,956 shares of its \$.004 par value Common Stock.

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## PART I - FINANCIAL INFORMATION

### Item 1. Financial Statements.

#### AAON, Inc., and Subsidiaries Consolidated Balance Sheets (unaudited)

March 31, 2008

(in thousands, except shares)

Assets	
Current assets:	
Cash and cash equivalents	\$ 5,474
Accounts receivable, net	36,502
Inventories, net	33,003
Prepaid expenses and other	567
Deferred tax assets	4,124
<hr/>	
Total current assets	79,670
Property, plant, and equipment	
Land	2,323
Buildings	32,340
Machinery and equipment	83,618
Furniture and fixtures	6,942
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Total property, plant and equipment	125,223
Less: Accumulated depreciation	66,010
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Property, plant and equipment, net	59,213
Notes receivable, long-term	75
<hr/>	
Total assets	\$ 138,958
<hr/>	
Liabilities and Stockholders' Equity	
Current liabilities:	
Current maturities of long-term debt	\$ 91
Accounts payable	15,457
Dividends payable	-
Accrued liabilities	19,530
<hr/>	
Total current liabilities	35,078
Long-term liabilities	216
Deferred tax liabilities	3,433
Commitments and contingencies	
Stockholders' equity:	
Preferred stock, \$.001 par value, 7,500,000 shares authorized, no shares issued	-
Common stock, \$.004 par value, 75,000,000 shares authorized, 17,976,956 and 18,054,246 issued and outstanding at March 31, 2008, and December 31, 2007, respectively	73
Additional paid-in capital	-
Accumulated other comprehensive income, net of tax	1,703
Retained earnings	98,455
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Total stockholders' equity	100,231
<hr/>	
Total liabilities and stockholders' equity	\$ 138,958

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The accompanying notes are an integral part of these statements.

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AAON, Inc., and Subsidiaries  
Consolidated Statements of Income  
(unaudited)

	Three Months March 31, 2008
	(in thousands, except per share amounts)
Net sales	\$ 65,456
Cost of sales	49,804
Gross profit	15,652
Selling, general and administrative expenses	5,902
Income from operations	9,750
Interest expense	(3)
Interest income	21
Other income	130
Income before income taxes	9,898
Income tax provision	3,464
Net income	\$ 6,434
Earnings per share:	
Basic	\$ 0.36
Diluted	\$ 0.35
Cash dividends declared per common share:	-
Weighted average shares outstanding:	
Basic	18,049
Diluted	18,311

\* Reflects three-for-two stock split effective August 21, 2007.

The accompanying notes are an integral part of these statements.

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### AAON, Inc., and Subsidiaries Consolidated Statements of Stockholders' Equity and Comprehensive Income (unaudited)

	Common Stock Shares	Amount	Paid-in Capital	Accumulated Other Comprehensive Income
(in thousands)				
Balance at December 31, 2007	18,054	\$ 73	\$ -	\$ 1,942
Comprehensive income:				
Net income	-	-	-	-
Foreign currency translation adjustment	-	-	-	(239)
Total comprehensive income				
Stock options exercised, including tax benefits	26	-	198	-
Share based compensation	-	-	241	-
Stock repurchased and retired	(103)	-	(439)	-
Balance at March 31, 2008	17,977	\$ 73	\$ -	\$ 1,703

The accompanying notes are an integral part of these statements.

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### AAON, Inc., and Subsidiaries Consolidated Statements of Cash Flows (unaudited)

	Three Months Ended March 31, 2008
(in thousands)	
OPERATING ACTIVITIES	
Net income	\$ 6,434
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation	2,457
Provision for losses on accounts receivable	26
Share-based compensation	241
Excess tax benefits from stock options exercised	(119)
Gain on disposition of assets	-
Deferred income taxes	(427)
Changes in assets and liabilities:	
Accounts receivable	2,212
Inventories, net	(1,199)
Prepaid expenses and other	(125)
Accounts payable	824
Accrued liabilities	(134)
Net cash provided by operating activities	10,190

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INVESTING ACTIVITIES	
Proceeds from sale of property, plant and equipment	-
Capital expenditures	(972)
Net cash used in investing activities	(972)
FINANCING ACTIVITIES	
Borrowings under revolving credit facility	4,219
Payments under revolving credit facility	(4,219)
Payments of long-term debt	(23)
Stock options exercised	79
Excess tax benefits from stock options exercised	119
Repurchase of stock	(1,823)
Cash dividends paid to stockholders	(2,943)
Net cash used in financing activities	(4,591)
Effect of exchange rate on cash	(32)
Net increase in cash and cash equivalents	4,595
Cash and cash equivalents, beginning of year	879
Cash and cash equivalents, end of period	\$ 5,474

The accompanying notes are an integral part of these statements.

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AAON, Inc., and Subsidiaries  
Notes to the Consolidated Financial Statements  
March 31, 2008  
(unaudited)

### 1. BASIS OF PRESENTATION

The financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to such rules and regulations. AAON, Inc. ("the Company") believes that the disclosures made in these financial statements are adequate to make the information presented not misleading when read in conjunction with the financial statements and the notes thereto included in the Company's latest audited financial statements which were included in the Form 10-K Report for the fiscal year ended December 31, 2007, filed by the Company with the SEC. In the opinion of management, the accompanying financial statements include all normal, recurring adjustments required for a fair presentation of the results of the periods presented. Operating results for the three months ended March 31, 2008, are not necessarily indicative of the results that may be expected for the year ending December 31, 2008.

#### Revenue Recognition

The Company recognizes revenues from sales of products when the products are shipped and the title and risk of ownership pass to the customer. Selling prices are fixed based on purchase orders or contractual agreements. Sales allowances and customer incentives are treated as reductions to sales and are provided for

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based on historical experiences and current estimates. For sales initiated by independent manufacturer representatives, the Company recognizes revenues net of the representatives' commission. The Company's policy is to record the collection and payment of sales taxes through a liability account.

### Common Stock Split

On July 12, 2007, the Company's Board of Directors approved a three-for-two stock split of the Company's outstanding stock for shareholders of record as of August 3, 2007. The stock split was treated as a 50% stock dividend which was distributed on August 21, 2007. The applicable share and per share data for all periods included herein has been restated to reflect the stock split.

### Currency

Foreign currency transactions and financial statements are translated in accordance with Financial Accounting Standards Board ("FASB") Statement 52, Foreign Currency Translations. The Company uses the U.S. dollar as its functional currency, except for the Canadian subsidiaries, which use the Canadian dollar. Adjustments arising from translation of the Canadian subsidiaries' financial statements are reflected in accumulated other comprehensive income. Transaction gains or losses that arise from exchange rate fluctuations applicable to transactions denominated in Canadian currency are included in the results of operations as incurred.

### New Accounting Pronouncements

In September 2006, the FASB released SFAS No. 157, Fair Value Measurements ("SFAS 157"). SFAS 157 defines fair value and establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Although SFAS 157 applies to (and amends) the provisions of existing authoritative literature, it does not, of itself, require any new fair value measurements or establish valuation standards. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Adoption of SFAS 157 did not have a material impact on the Company's Consolidated Financial Statements.

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In February, 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, which creates an alternative measurement treatment for certain financial assets and financial liabilities. SFAS 159 permits fair value to be used for both the initial and subsequent measurements on an instrument by instrument basis, with changes in the fair value to be recognized in earnings as those changes occur. This election is referred to as the fair value option. SFAS 159 also requires additional disclosures to compensate for the lack of comparability that will arise from the use of the fair value option. SFAS 159 is effective for fiscal years beginning after November 15, 2007. Adoption of SFAS 159 did not have a material impact on the Company's Consolidated Financial Statements. The Company did not elect the fair value option for any assets or liabilities.

## 2. ACCOUNTS RECEIVABLE

The Company grants credit to its customers and performs ongoing credit evaluations. The Company generally does not require collateral or charge interest. The Company establishes an allowance for doubtful accounts based upon factors surrounding the credit risk of specific customers, historical trends, economic and market conditions and the age of the receivable. Past due accounts

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are generally written off against the allowance for doubtful accounts only after all collection attempts have been exhausted.

Accounts receivable and the related allowance for doubtful accounts are as follows:

	March 31, 2008	December 2007
	-----	
	(in thousands)	
Accounts receivable	\$ 36,809	\$ 39,000
Less: Allowance for doubtful accounts	(307)	
	-----	
Total, net	\$ 36,502	\$ 38,693
	=====	

	March 31, 2008	Three Months Ended March 31, 2008	March 31, 2007
	-----		
	(in thousands)		
Allowance for doubtful accounts:			
Balance, beginning of period	\$ 407		\$ 407
Provision for losses on accounts receivable	160		
Adjustments to provision	(134)		
Accounts receivable written off, net of recoveries	(126)		
	-----		
Balance, end of period	\$ 307		\$ 307
	=====		

3. INVENTORIES

Inventories are valued at the lower of cost or market. Cost is determined by the first-in, first-out (FIFO) method. The Company establishes an allowance for excess and obsolete inventories based on product line changes, the feasibility of substituting parts and the need for supply and replacement parts. Inventory balances at March 31, 2008 and December 31, 2007, and the related changes in the allowance for excess and obsolete inventories account for the three months ended March 31, 2008 and 2007 are as follows:

	March 31, 2008	December 2007
	-----	
	(in thousands)	
Raw materials	\$ 28,322	\$ 27,000
Work in process	1,550	1,500
Finished goods	3,481	2,500
	-----	
Less: Inventory reserve	33,353	32,000
	(350)	
	-----	

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Total, net \$ 33,003 \$ 31

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	Three Months Ended March 31, 2008	March 20
----- (in thousands) -----		
Allowance for excess and obsolete inventories:		
Balance, beginning of period	\$ 350	\$
Provision for excess and obsolete inventories	-	
Adjustments to reserve	-	
	-----	-----
Balance, end of period	\$ 350	\$
	=====	=====

4. ACCRUED LIABILITIES

At March 31, 2008 and December 31, 2007, accrued liabilities were comprised of the following:

	March 31, 2008	December 31, 2007
----- (in thousands) -----		
Warranty	\$ 6,420	\$ 6,308
Commissions	7,326	8,851
Payroll	3,060	2,175
Workers' compensation	1,129	1,127
Medical self-insurance	580	608
Other	1,015	345
	-----	-----
Total	\$ 19,530	\$ 19,414
	=====	=====

5. SUPPLEMENTAL CASH FLOW INFORMATION

Interest payments of \$3,000 and \$10,000 were made for the three months ended March 31, 2008 and 2007, respectively. Payments for income taxes of \$2.0 million and \$0 were made during the three months ended March 31, 2008 and 2007, respectively. Dividends payable of \$2.9 million were accrued as of December 31, 2007. These dividends were paid in January 2008.

6. REVOLVING CREDIT FACILITY

The Company's revolving credit facility provides for maximum borrowings of \$15.2 million which is provided by the Bank of Oklahoma, National Association. Under the line of credit, there is one standby letter of credit totaling approximately \$1.3 million. The letter of credit is a requirement of the Company's workers compensation insurance and has been renewed and will expire December 31, 2008. Interest on borrowings is payable monthly at the Wall Street Journal prime rate less 0.5% or LIBOR plus 1.6%, at the election of the Company (4.71% at March 31, 2008). No fees are associated with the unused portion of the committed amount. At March 31, 2008 and December 31, 2007, the Company had no borrowings outstanding under the revolving credit facility. Borrowings available under the



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revolving credit facility at March 31, 2008, were \$13.9 million. The credit facility requires the Company to maintain certain financial ratios. At March 31, 2008, the Company was in compliance with its financial ratio covenants. On July 30, 2007 the Company renewed the line of credit with a maturity date of July 30, 2008.

### 7. STOCK COMPENSATION

The Company maintains a stock option plan for key employees, directors and consultants. The Company's stock option plan provided for 4.4 million shares of common stock to be issued under the plan. Under the terms of the plan, the exercise price of shares granted may not be less than 85% of the fair market value at the date of the grant. Options granted to directors prior to May 25, 2004, vest one year from the date of grant and are exercisable for nine years thereafter. Options granted to directors on or after May 25, 2004, vest one-third each year, commencing one year after the date of grant. All other options granted vest at a rate of 20% per year, commencing one year after date of grant, and are exercisable during years 2-10. On May 22, 2007, the stockholders of the Company adopted a Long-Term Incentive Plan which provides an additional 750,000 shares that can be granted in the form of stock options, stock appreciation rights, restricted stock awards, performance units and performance awards. Since inception of the Plan, non-qualified stock options and restricted stock awards have been granted with the same vesting schedule as the previous plan.

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The Company applies the fair value recognition provisions of Statement of Financial Accounting Standards No. 123(R) Share-Based Payment ("SFAS 123R"). The compensation cost is based on the grant date fair value of stock options issued calculated using a Black-Scholes-Merton Option Pricing Model, or the grant date fair value of a restricted share, in accordance with provisions of SFAS 123R.

For the three month periods ended March 31, 2008 and 2007, the Company recognized approximately \$124,000 and \$159,000, respectively, in pre-tax compensation expense related to stock options in the Consolidated Statements of Income. The total pre-tax compensation cost related to unvested stock options and unvested restricted stock not yet recognized as of March 31, 2008, is \$1.4 million and is expected to be recognized over a weighted-average period of 2.2 years.

The following assumptions were used to determine the fair value of the unvested stock options on the original grant date for expense recognition purposes for options granted during the three months ended March 31, 2007 and 2008.

	Three Months Ended	
	March 31, 2008	March 31, 2007
<b>Directors and Officers:</b>		
Expected dividend yield	1.81%	N/A
Expected volatility	43.52%	N/A
Risk-free interest rate	2.84%	N/A
Expected life	8.0 yrs	N/A
Forfeiture Rate	0%	N/A
<b>Employees:</b>		
Expected dividend yield	1.81%	1.76%
Expected volatility	42.55%	42.34%
Risk-free interest rate	2.84%	4.74%
Expected life	6.3 yrs	6.3 yrs
Forfeiture Rate	28%	28%

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The expected term of the options is based on evaluations of historical and expected future employee exercise behavior. The risk-free interest rate is based on the U.S. Treasury rates at the date of grant with maturity dates approximately equal to the expected life at the grant date. Volatility is based on historical volatility of the Company's stock. The Company initiated a dividend payout in the second quarter of 2006. Previously, the Company used Board of Director approved semi-annual dividend payouts of \$0.20 per share through July 3, 2007, to calculate the expected dividend yield. The Board of Directors has approved future dividend payments of \$0.16 per share and the table above was adjusted to reflect the rate change.

A summary of stock options outstanding as of March 31, 2008, is as follows:

Range of Exercise Prices	Options Outstanding			
	Number Outstanding at March 31, 2008	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Aggregate Intrinsic Value
\$2.67 - \$3.85	307,320	1.09	\$ 3.20	\$ 16.83
\$5.73 - \$11.29	240,913	4.58	8.44	11.59
\$11.40 - \$12.00	46,500	7.34	11.69	8.34
\$12.68 - \$15.55	60,000	7.55	14.27	5.76
\$15.99 - \$21.01	258,650	8.69	17.25	2.78
Total	913,383	4.91	\$ 9.72	\$ 13.53

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A summary of option activity as of March 31, 2008, is as follows:

Stock Options	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term
Outstanding at January 1, 2008	928,933	\$ 9.47	
Granted	24,000	16.96	
Exercised	(23,950)	3.31	
Forfeited or Expired	(15,600)	15.56	
Outstanding at March 31, 2008	913,383	9.72	4.91
Exercisable at March 31, 2008	589,933	\$ 6.50	3.05

The weighted average grant date fair value of options granted during the three months ended March 31, 2008 and 2007 was \$6.69 and \$7.22, respectively. The

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total intrinsic value of options exercised during the three months ended March 31, 2008 and 2007 was approximately \$342,000 and \$4.1 million, respectively. The cash received from options exercised during the three months ended March 31, 2008 and 2007, was approximately \$79,000 and \$0.7 million, respectively. The impact of these cash receipts is included in financing activities in the accompanying Consolidated Statements of Cash Flows.

A summary of the unvested stock options for the three month period ended March 31, 2008, is as follows:

	Shares	Weighted Average Grant Date Fair Value
	-----	-----
Unvested at January 1, 2008	335,300	\$ 6.49
Granted	24,000	6.69
Vested	(20,250)	5.82
Forfeited	(15,600)	6.29
	-----	-----
Unvested at March 31, 2008	323,450	\$ 6.56
	=====	=====

The Company also grants restricted stock awards to employees and directors. These awards are recorded at their fair values on the date of grant and compensation cost is recorded using straight-line vesting over the service period. For the three months ended March 31, 2008, the Company recognized approximately \$117,000, in pre-tax compensation expense related to restricted stock awards in the Consolidated Statements of Income. In addition, as of March 31, 2008, unrecognized compensation cost related to non-vested restricted stock awards was approximately \$617,000 which is expected to be recognized over a weighted average period of 1.9 years.

During 2007, the Compensation Committee of the Board of Directors authorized and issued restricted stock to the officers and directors of the Company. The restricted stock award program offers the opportunity to earn shares of AAON common stock over time, rather than options that give the right to purchase stock at a set price. Restricted stock granted to directors vest one-third each year. All other restricted stock vest at a rate of 20% per year. Restricted stock awards are grants that entitle the holder to shares of common stock subject to certain terms. The fair value of restricted stock grants is based on the fair market value of AAON common stock on the respective grant dates, reduced for the present value of dividends.

### 8. EARNINGS PER SHARE

Basic net income per share is calculated by dividing net income by the weighted average number of shares of common stock outstanding during the period. Diluted net income per share assumes the conversion of all potentially dilutive securities and is calculated by dividing net income by the sum of the weighted average number of shares of common stock outstanding plus all potentially dilutive securities. Dilutive common shares consist primarily of stock options and restricted stock.

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	Three Months Ended
	March 31, 2008                      March 31, 2007
	-----

(in thousands, except share and per share data)

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Numerator:

Net income	\$ 6,434	\$ 6,317
	=====	=====

Denominator:

Denominator for basic earnings per share- Weighted average shares	18,048,683	18,561,096*
----------------------------------------------------------------------	------------	-------------

Effect of dilutive employee stock options and restricted stock awards	262,402	341,175*
	-----	-----

Denominator for diluted earnings per share- Weighted average shares	18,311,085	18,902,271*
------------------------------------------------------------------------	------------	-------------

Earnings per share:

Basic	\$ 0.36	\$ 0.34*
	=====	=====

Diluted	\$ 0.35	\$ 0.33*
	=====	=====

Anti-dilutive shares	302,150	298,500*
	=====	=====

Weighted average exercise price	\$ 16.87	\$ 16.61*
	=====	=====

\*Reflects three-for-two stock split effective August 21, 2007

9. INCOME TAXES

The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction, and various state and foreign jurisdictions. Effective January 1, 2007, the Company adopted FIN 48. The total amount of unrecognized tax benefits at March 31, 2008, is \$8,000 related to tax positions for which it is reasonably possible that the total amounts could significantly decrease during the next twelve months. This amount represents the unrecognized tax benefits comprised of items related to determination of state nexus. Resolution of these tax benefits will occur through a voluntary compliance program, which was initiated during 2007.

The Company recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. At March 31, 2008, the Company had accrued \$8,000 and \$0 for the potential payment of interest and penalties, respectively.

As of March 31, 2008, the Company is subject to U.S. Federal income tax examinations for the tax years 2005 through 2007, and to non-U.S. income tax examinations for the tax years of 2005 through 2007. In addition, the Company is subject to state and local income tax examinations for the tax years 2002 through 2007.

The total amount of unrecognized tax benefits that if recognized would affect the effective tax rate is \$20,000.

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10. STOCK REPURCHASE

Following repurchases of approximately 12% of its outstanding Common Stock

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between September 1999 and September 2001, the Company announced and began another stock repurchase program on October 17, 2002, targeting repurchases of up to an additional 10% (2.0 million shares) of its outstanding stock. On February 14, 2006, the Board of Directors approved the suspension of the Company's repurchase program. Through February 14, 2006, the Company had repurchased a total of 1,886,796 shares under this program for an aggregate price of \$22,034,568, or an average price of \$11.68 per share. The Company purchased the shares at the then current market price.

On November 6, 2007, the Board authorized a new stock buyback program, targeting repurchases of up to approximately 10% (1.8 million shares) of the outstanding stock of the Company from time to time in open market transactions at prevailing market prices. The Company purchases the shares at the current market price. Through March 31, 2008, the Company repurchased a total of 771,100 shares under this program for an aggregate price of \$14,441,824, or an average price of \$18.73 per share.

On July 1, 2005, the Company entered into a stock repurchase arrangement by which employee-participants in AAON's 401(k) savings and investment plan are entitled to have shares of AAON stock in their accounts sold to the Company to provide diversification of their investments. The maximum number of shares to be repurchased is unknown under the program as the amount is contingent on the number of shares sold by employees. Through March 31, 2008, the Company repurchased 523,316 shares for an aggregate price of \$8,108,892, or an average price of \$15.50 per share. The Company purchases the shares at the current market price.

On November 7, 2006, the Board of Directors authorized the Company to repurchase shares from certain directors following their exercise of stock options. The maximum number of shares to be repurchased is unknown under the program as the amount is contingent on the number of shares sold by directors. Through March 31, 2008, the Company repurchased 260,625 shares for an aggregate price of \$5,232,188, or an average price of \$20.08 per share. The Company purchases the shares at the current market price.

### 11. CONTINGENCIES

The Company is subject to claims and legal actions that arise in the ordinary course of business. Management believes that the ultimate liability, if any, will not have a material effect on the Company's results of operations or financial position.

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

AAON, Inc. ("the Company") engineers, manufactures and markets air-conditioning and heating equipment consisting of standardized and custom rooftop units, chillers, air-handling units, make-up units, heat recovery units, condensing units, coils and boilers. Custom units are marketed and sold to retail, manufacturing, educational, medical and other commercial industries. AAON markets units to all 50 states in the United States and certain provinces in Canada. International sales are less than five percent as the majority of all sales are domestic.

The Company sells its products to property owners and contractors through a network of manufacturers' representatives and its internal sales force. Demand for the Company's products is influenced by national and regional economic and demographic factors. The commercial and industrial new construction market is subject to cyclical fluctuations in that it is generally tied to housing starts,

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but has a lag factor of 6-18 months. Housing starts, in turn, are affected by such factors as interest rates, the state of the economy, population growth and the relative age of the population. When new construction is down, the Company emphasizes the replacement market.

The principal components of cost of goods sold are labor, raw materials, component costs, factory overhead, freight out and engineering expense. The principal raw materials used in AAON's manufacturing processes are steel, copper and aluminum. Raw materials ranged in prices and at times increases were incurred up to approximately 45% for steel, 40% for aluminum and 85% for copper from 2006 to 2008. The Company reviewed and adjusted current pricing strategies and created efficiencies in production and continued relationships with suppliers in order to mitigate the economic factors of increasing commodity prices. The major component costs include compressors, electric motors and electronic controls, which also increased due to increases in commodities.

Selling, general, and administrative ("SG&A") costs include the Company's internal sales force, warranty costs, profit sharing and administrative expense. Warranty expense is estimated based on historical trends and other factors. The Company's warranty on its products is: for parts only, the earlier of one year from the date of first use or 18 months from date of shipment; compressors (if applicable), an additional four years; on gas-fired heat exchangers (if applicable), 15 years; and on stainless steel heat exchangers (if applicable), 25 years. Warranty charges on heat exchangers occur infrequently.

The office facilities of the Company consist of a 337,000 square foot building (322,000 sq. ft. of manufacturing/warehouse space and 15,000 sq. ft. of office space) located at 2425 S. Yukon Avenue, Tulsa, Oklahoma (the "original facility"), and a 563,000 square foot manufacturing/warehouse building and a 22,000 square foot office building ("the expansion facility") located across the street from the original facility at 2440 S. Yukon Avenue. The Company utilizes 39% of the expansion facility and the remaining 61% is leased to a third party.

Other operations are conducted in a plant/office building at 203-207 Gum Springs Road in Longview, Texas, containing 258,000 square feet (251,000 sq. ft. of manufacturing/warehouse and 7,000 sq. ft. of office space). An additional 15 acres of land was purchased for future expansion in 2004 and 2005 in Longview, Texas.

The Company's operations in Burlington, Ontario, Canada, are located at 279 Sumach Drive, consisting of an 82,000 sq. ft. office/manufacturing facility on a 5.6 acre tract of land.

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Set forth below is unaudited income statement information with respect to the Company for the periods ended March 31, 2008 and 2007:

	Three Months Ended			
	March 31, 2008		March 31, 2007	
-----				
(In thousands)				
Net sales	\$ 65,456	100.0%	\$ 58,628	100.0%
Cost of sales	49,804	76.1%	42,906	73.2%
Gross profit	15,652	23.9%	15,722	26.8%
-----				

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Selling, general and administrative expenses	5,902	9.0%	5,747	9.8%
Income from operations	9,750	14.9%	9,975	17.0%
Interest expense	(3)	0.0%	(10)	0.0%
Interest income	21	0.0%	3	0.0%
Other income	130	0.2%	188	0.3%
Income before income taxes	9,898	15.1%	10,156	17.3%
Income tax provision	3,464	5.3%	3,839	6.5%
Net income	\$ 6,434	9.8%	\$ 6,317	10.8%

### Results of Operations

Key events impacting our cash balance, financial condition, and results of operations for the three months ended March 31, 2008, include the following:

- o An increase in the volume of sales on all product lines due to commercial construction growth and market share gains, and effective moderation of commodity costs with purchase agreements and pricing strategies.
- o AAON remained the leader in the industry for environmentally-friendly, energy efficient and quality innovations, utilizing R410A refrigerant and phasing out pollutant causing R22 refrigerant. The phase out of R22 began at the beginning of 2004. AAON also utilizes a high performance composite foam panel to eliminate over half of the heat transfer from typical fiberglass insulated panels. AAON continues to utilize sloped condenser coils, and access compartments to filters, motor, and fans. All of these innovations increase the demand for AAON's products thus increasing market share
- o In February 2006, the Board of Directors initiated a program of semi-annual cash dividend payments. Cash payments of \$5.0 million were made in 2007, and \$2.9 million were made in January 2008.
- o Stock repurchases of AAON stock from employee's 401(k) savings and investments plan was authorized in 2005. Stock repurchases of AAON stock from directors was authorized in 2006. Stock repurchases of AAON stock from the open market was authorized in 2007. Total purchases resulted in cash payments of \$1.8 million. This cash outlay is partially offset by cash received from options exercised by employees as a part of an incentive bonus program. The cash received in the first three months of 2008 from options exercised was approximately \$79,000.
- o Purchases of equipment to create efficiencies remained a priority. AAON's capital expenditures were \$1.0 million. Equipment purchases create significant efficiencies, lower production costs and allow continued growth in production. The Company currently estimates it will spend approximately \$7.0 million to \$10.0 million on capital expenditures in 2008 for continued growth.

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### Net Sales

Net sales increased \$6.9 million, or 11.8%, to \$65.5 million from \$58.6 million for the three months ended March 31, 2008, compared to the same period in 2007. Increased sales were attributable to an increase in volume of product sold

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related to the Company's new and redesigned products being favorably received by its customers, active marketing by sales representatives and from certain pricing strategies implemented on 90% of the Company's product lines. Management anticipates continued growth throughout 2008.

### Gross Profit

Gross profit was \$15.7 million for both the three months ended March 31, 2008 and 2007, respectively. As a percentage of sales, gross margins were 23.9% compared to 26.8% for the three months ended March 31, 2008 and 2007, respectively. The decrease in gross margins for the three months ended March 31, 2008, compared to the same period in 2007, was a result of higher cost of sales primarily due to increases in manufacturing expenses.

Steel, copper and aluminum are high volume materials used in the manufacturing of the Company's products, which are obtained from domestic suppliers. Raw materials ranged in prices and at times increases were incurred up to approximately 45% for steel, 40% for aluminum and 85% for copper from 2006 to 2008, causing increased inventory costs. The Company also purchases from other domestic manufacturers certain components, including compressors, electric motors and electrical controls used in its products. The suppliers of these components are significantly affected by the rising raw material costs, as steel, copper and aluminum are used in the manufacturing of their products; therefore, the Company is also experiencing price increases from component part suppliers. The Company continues to monitor these costs and price units accordingly. The Company instituted several price increases to customers from 2005 to 2008 in an attempt to offset the continued increases in steel, copper and aluminum. The Company attempts to limit the impact of price increases on these materials by entering into cancelable fixed price contracts with its major suppliers for periods of 6-12 months.

### Selling, General and Administrative Expenses

Selling, general and administrative expenses increased to \$5.9 million from \$5.7 million, a change of approximately \$0.2 million, or 3.5%, for the three months ended March 31, 2008, compared to the same period in 2007. The increase for the three months ended March 31, 2008, was primarily caused by an increase in selling related expenses and an overall increase in general and administrative expenses.

### Other Income

Other income was \$0.1 million and \$0.2 million for the three months ended March 31, 2008 and 2007, respectively. Other income is attributable primarily to rental income from the Company's expansion facility. All expenses associated with the facility that are allocated to the rental portion of the building are included in other income. The Company plans to continue to rent the expansion facility until it is needed for increased capacity. Other income also includes foreign currency gains and losses that result from operations in Canada.

### Analysis of Liquidity and Capital Resources

AAON's working capital and capital expenditure requirements are generally met through net cash provided by operations and the revolving bank line of credit.

**Cash Flows Provided by Operating Activities.** Net cash provided by operating activities increased in the three months ended March 31, 2008 by \$3.5 million from the three months ended March 31, 2007. The increase was due primarily to changes in inventories and accrued liabilities.

**Cash Flows Used in Investing Activities.** Cash flows used in investing activities were \$1.0 million and \$4.5 million for the three months ended March 31, 2008 and



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2007, respectively. The decrease in cash flows used in investing activities in 2008 was primarily related to lower capital expenditures of \$1.0 million for additions to manufacturing facilities, machinery and equipment compared to \$4.5 million for the same period in 2007. Capital expenditures in 2007 related to building renovations and machinery and equipment to further automate production. Management utilizes cash flows provided from operating activities to fund capital expenditures that are expected to spur growth and create efficiencies. The Company is currently in line with budgeted capital expenditures of approximately \$7.0 million to \$10.0 million in 2008 for equipment requirements. The Company expects its cash requirements to be provided from cash flows from operations.

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**Cash Flows Used in Financing Activities.** Cash flows used in financing activities were \$4.6 million and \$1.9 million for the three months ended March 31, 2008 and 2007, respectively. The increase of cash used in financing activities primarily relates to cash dividends declared and paid and the continued repurchase of the Company's stock.

The Company repurchased shares of stock from employees' 401(k) savings and investment plan and other incentive plans and the open market for the three months ended March 31, 2008, in the amount of approximately \$1.8 million for 103,040 shares of stock. There were shares of stock repurchased for a total of \$1.6 million for the same period in 2007.

The Company received cash from stock options exercised of approximately \$79,000 and classified the tax benefit of stock options exercised of approximately \$119,000 in financing activities for the three months ended March 31, 2008. The cash received for options exercised and income tax effect partially offset the stock repurchase and dividend payments for the three months ended March 31, 2008. The cash received from stock options exercised for the same period in 2007 was \$0.7 million and the tax benefit of stock options exercised was \$1.6 million.

In February 2006, the Board of Directors authorized a semi-annual cash dividend payment. Cash dividends were declared in December 2007 and were paid in January 2008 in the amount of \$2.9 million. Prior to 2006, no cash dividends had been declared or paid. Board of Director approval is required to determine the date of declaration for each semi-annual payment.

On July 12, 2007, the Company's Board of Directors approved a three-for-two stock split of AAON's outstanding stock for shareholders of record as of August 3, 2007. The stock split was treated as a 50% stock dividend which was distributed on August 21, 2007. As a result of the stock split, the Company adjusted the dividend paid per share to \$0.16. The applicable share and per share data for all periods included herein has been restated to reflect the stock split.

### General

The Company's revolving credit facility provides for maximum borrowings of \$15.2 million which is provided by the Bank of Oklahoma, National Association. Under the line of credit, there is one standby letter of credit totaling approximately \$1.3 million. The letter of credit is a requirement of the Company's workers compensation insurance and has been renewed and will expire December 31, 2008. Interest on borrowings is payable monthly at the Wall Street Journal prime rate less 0.5% or LIBOR plus 1.6%, at the election of the Company (4.71% at March 31, 2008). No fees are associated with the unused portion of the committed amount. At March 31, 2008 and December 31, 2007, the Company had no borrowings outstanding under the revolving credit facility. Borrowings available under the

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revolving credit facility at March 31, 2008, were \$13.9 million. The credit facility requires the Company to maintain certain financial ratios. At March 31, 2008, the Company was in compliance with its financial ratio covenants. On July 30, 2007, the line of credit's maturity date was extended to July 30, 2008.

Management believes the Company's bank revolving credit facility, or comparable financing, and projected cash flows from operations will provide the necessary liquidity and capital resources to the Company for fiscal year 2008 and the foreseeable future. The Company's belief that it will have the necessary liquidity and capital resources is based upon its knowledge of the heating, ventilation, and air conditioning ("HVAC") industry and its place in that industry, its ability to limit the growth of its business if necessary, its ability to authorize dividend cash payments, and its relationship with its existing bank lender. For information concerning the Company's revolving credit facility at March 31, 2008, see Note 6 to the Consolidated Financial Statements, Revolving Credit Facility.

### Critical Accounting Policies

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Because these estimates and assumptions require significant judgment, future actual results could differ from those estimates and could have a significant impact on the Company's results of operations, financial position and cash flows. The Company reevaluates its estimates and assumptions on a monthly basis.

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There have been no significant changes in critical accounting policies or management estimates since the year ended December 31, 2007. A comprehensive discussion of the Company's critical accounting policies and management estimates is included in Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

### New Accounting Pronouncements

In September 2006, the FASB released SFAS No. 157, Fair Value Measurements ("SFAS 157"). SFAS 157 defines fair value and establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. Although SFAS 157 applies to (and amends) the provisions of existing authoritative literature, it does not, of itself, require any new fair value measurements or establish valuation standards. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. Adoption of SFAS 157 did not have a material impact on the Company's Consolidated Financial Statements.

In February, 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, which creates an alternative measurement treatment for certain financial assets and financial liabilities. SFAS 159 permits fair value to be used for both the initial and subsequent measurements on an instrument by instrument basis, with changes in the fair value to be recognized in earnings as those changes occur. This election is referred to as the fair value option. SFAS 159 also requires additional disclosures to compensate for the lack of comparability that will arise from the use of the fair value option. SFAS 159 is effective for fiscal years beginning

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after November 15, 2007. Adoption of SFAS 159 did not have a material impact on the Company's Consolidated Financial Statements. The Company did not elect the fair value option for any assets or liabilities.

### Forward-Looking Statements

This Quarterly Report on Form 10-Q includes "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "expects", "anticipates", "intends", "plans", "believes", "seeks", "estimates", "will", and variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date on which they are made. The Company undertakes no obligation to update publicly any forward-looking statements, whether as a result of new information, future events or otherwise. Important factors that could cause results to differ materially from those in the forward-looking statements include (1) the timing and extent of changes in raw material and component prices, (2) the effects of fluctuations in the commercial/industrial new construction market, (3) the timing and extent of changes in interest rates, as well as other competitive factors during the year, and (4) general economic, market or business conditions.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk.

The Company is subject to interest rate risk on its revolving credit facility which bears variable interest based upon a prime or LIBOR rate. The Company had no outstanding balance as of March 31, 2008.

Foreign sales accounted for less than 5% of the Company's sales for the three months ended March 31, 2008, and the Company accepts payment for such sales in U.S. and Canadian dollars; therefore, the Company believes it is not exposed to significant foreign currency exchange rate risk on these sales. Foreign currency transactions and financial statements are translated in accordance with FASB Statement No. 52, Foreign Currency Translation. The Company uses the U.S. dollar as its functional currency, except for the Canadian subsidiaries, which use the Canadian dollar. Adjustments arising from translation of the Canadian subsidiaries' financial statements are reflected in accumulated other comprehensive income in the Consolidated Statements of Stockholders' Equity and Comprehensive Income. Transaction gains or losses that arise from exchange rate fluctuations applicable to transactions are denominated in Canadian currency and are included in the results of operations as incurred. The exchange rate of the United States dollar to the Canadian dollar was \$0.9882 and \$0.8637 at March 31, 2008 and 2007, respectively.

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Important raw materials purchased by the Company are steel, copper and aluminum, which are subject to price fluctuations. The Company attempts to limit the impact of price increases on these materials by entering cancelable fixed price contracts with its major suppliers for periods of 6 -12 months, however; in 2007 cost increases in basic commodities, such as steel, copper and aluminum, severely impacted profit margins. Continued volatility in prices may impact profit margins in future periods.

The Company does not utilize derivative financial instruments to hedge its interest rate or raw materials price risks.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

At the end of the period covered by this Quarterly Report on Form 10-Q, the Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer believe that:

- o The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports it files under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms; and
- o The Company's disclosure controls and procedures operate such that important information flows to appropriate collection and disclosure points in a timely manner and are effective to ensure that such information is accumulated and communicated to the Company's management, and made known to the Company's Chief Executive Officer and Chief Financial Officer, particularly during the period when this Quarterly Report was prepared, as appropriate to allow timely decisions regarding the required disclosure.

AAON's Chief Executive Officer and Chief Financial Officer have evaluated the Company's disclosure controls and procedures and concluded that these controls and procedures were effective as of March 31, 2008.

Changes in Internal Control over Financial Reporting

There have been no changes in internal control over financial reporting that occurred during 2008 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1A. Risk Factors.

There have been no material changes from risk factors as previously disclosed in the Company's Form 10-K in response to Item 1A, to Part I of its Form 10-K.

Item 2. Unregistered Sales of Equity and Securities and Use of Proceeds.

Following repurchases of approximately 12% of its outstanding Common Stock between September 1999 and September 2001, the Company announced and began another stock repurchase program on October 17, 2002, targeting repurchases of up to an additional 10% (2.0 million shares) of its outstanding stock. On February 14, 2006, the Board of Directors approved the suspension of the Company's repurchase program. Through February 14, 2006, the Company had repurchased a total of 1,886,796 shares under this program for an aggregate price of \$22,034,568, or an average price of \$11.68 per share. The Company purchased the shares at the then current market price.

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On November 6, 2007, the Board authorized a new stock buyback program, targeting repurchases of up to approximately 10% (1.8 million shares) of the outstanding stock of the Company from time to time in open market transactions at prevailing market prices. Through March 31, 2008, the Company repurchased a total of 771,100 shares under this program for an aggregate price of \$14,441,824, or an average price of \$18.73 per share.

On July 1, 2005, the Company entered into a stock repurchase arrangement by which employee-participants in AAON's 401(k) savings and investment plan are entitled to have shares of AAON's stock in their accounts sold to the Company to provide diversification of their investments. The maximum number of shares to be repurchased is unknown under the program as the amount is contingent on the number of shares sold by employees. Through March 31, 2008, the Company repurchased 523,316 shares for an aggregate price of \$8,108,892, or an average price of \$15.50 per share. The Company purchases the shares at the current market price.

On November 7, 2006, the Board of Directors authorized the Company to repurchase shares from certain directors following their exercise of stock options. The maximum number of shares to be repurchased is unknown under the program as the amount is contingent on the number of shares sold by directors. Through March 31, 2008, the Company has repurchased 260,625 shares for an aggregate price of \$5,232,188, or an average price of \$20.08 per share. The Company purchases the shares at the current market price.

Repurchases during the first quarter of 2008 were as follows:

### ISSUER PURCHASES OF EQUITY SECURITIES

Period	(a) Total Number of Shares (or Units) Purchased	(b) Average Price Paid Per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
January 2008	9,288	\$ 17.48	9,288	-
February 2008	7,235	\$ 17.39	7,235	-
March 2008	86,517	\$ 17.78	86,517	-
Total	103,040	\$ 17.72	103,040	-

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

None

Item 5. Other Information.

None

Item 6. Exhibits.

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(a) Exhibits

(i)	Exhibit 31.1	Section 302 Certification of CEO
(ii)	Exhibit 31.2	Section 302 Certification of CFO
(iii)	Exhibit 32.1	Section 1350 Certification of CEO
(iv)	Exhibit 32.2	Section 1350 Certification of CFO

SIGNATURES

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

AAON, INC.

Dated: May 6, 2008

By: /s/ Norman H. Asbjornson

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Norman H. Asbjornson  
President/CEO

Dated: May 6, 2008

By: /s/ Kathy I. Sheffield

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Kathy I. Sheffield  
Vice President/CFO