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

# FORM 10-Q

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

For the quarterly period ended **June 30, 2020**

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

For the transition period from ________________________ to ______________________

Commission File Number **000-51372**

**Omega Flex, Inc.**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Pennsylvania** | **23-1948942** |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| **451 Creamery Way, Exton, PA** | **19341** |
| (Address of principal executive offices) | (Zip Code) |

**(610) 524-7272**

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 [**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, non-accelerated filer, or a smaller reporting company filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange. (Check one):

Large accelerated filer [ ] Accelerated filer [**x**] 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**]

| Title of each class | Trading Symbol | Name of each exchange on which registered |
|---|---|---|
| Common Stock, par value $0.01 per share | OFLX | NASDAQ Global Market |

**APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY PROCEEDINGS DURING THE PRECEDING FIVE YEARS.**

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

The number of shares of the registrant's common stock outstanding as of June 30, 2020 was 10,094,322.

**OMEGA FLEX, INC.**
**QUARTERLY REPORT ON FORM 10-Q**
**FOR THE SIX MONTHS ENDED JUNE 30, 2020**

**INDEX**

## PART I - FINANCIAL INFORMATION

### Item 1 - Financial Statements

**OMEGA FLEX, INC.**
**CONDENSED CONSOLIDATED BALANCE SHEETS**
**(Amounts in Thousands, Except Share Amounts)**

| | June 30, 2020 (unaudited) | December 31, 2019 |
|---|---|---|
| **ASSETS** | | |
| Current Assets: | | |
| Cash and Cash Equivalents | $19,487 | $16,098 |
| Accounts Receivable - less allowances of $887 and $1,433, respectively | 14,113 | 17,047 |
| Inventories - Net | 11,083 | 11,078 |
| Other Current Assets | 974 | 2,097 |
| Total Current Assets | 45,657 | 46,320 |
| Right-Of-Use Assets - Operating | 589 | 771 |
| Property and Equipment - Net | 8,660 | 8,909 |
| Goodwill - Net | 3,526 | 3,526 |
| Deferred Taxes | 4 | 4 |
| Other Long Term Assets | 1,481 | 1,454 |
| Total Assets | $59,917 | $60,984 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Current Liabilities: | | |
| Accounts Payable | $2,155 | $2,383 |
| Accrued Compensation | 2,337 | 4,618 |
| Accrued Commissions and Sales Incentives | 2,846 | 4,461 |
| Dividends Payable | 2,827 | 2,826 |
| Taxes Payable | 2,858 | 423 |
| Lease Liability - Operating | 311 | 369 |
| Other Liabilities | 4,212 | 5,404 |
| Total Current Liabilities | 17,546 | 20,484 |
| Lease Liability – Operating, net of current portion | 291 | 418 |
| Deferred Taxes | 186 | 331 |
| Long Term Taxes Payable | 559 | --- |
| Other Long Term Liabilities | 1,673 | 2,175 |
| Total Liabilities | 20,255 | 23,408 |
| Commitments and Contingencies (Note 5) | | |
| Shareholders' Equity: | | |
| Omega Flex, Inc. Shareholders' Equity: | | |
| Common Stock – par value $0.01 share: authorized 20,000,000 shares: 10,153,633 shares issued and 10,094,322 outstanding at both June 30, 2020 and December 31, 2019 | 102 | 102 |
| Treasury Stock | (1) | (1) |
| Paid-in Capital | 11,025 | 11,025 |
| Retained Earnings | 29,427 | 27,165 |
| Accumulated Other Comprehensive Loss | (1,091) | (909) |
| Total Omega Flex, Inc. Shareholders' Equity | 39,462 | 37,382 |
| Noncontrolling Interest | 200 | 194 |
| Total Shareholders' Equity | 39,662 | 37,576 |
| Total Liabilities and Shareholders' Equity | $59,917 | $60,984 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

# OMEGA FLEX, INC.
## CONDENSED CONSOLIDATED STATEMENTS OF INCOME
**(Amounts in Thousands, Except Per Share and Share Amounts)**

| | For the three months ended June 30, | | For the six months ended June 30, | |
|---|---|---|---|---|
| | 2020 | 2019 | 2020 | 2019 |
| | (Unaudited) | | | |
| Net Sales | $ 21,818 | $ 26,809 | $ 47,084 | $ 53,597 |
| Cost of Goods Sold | 8,556 | 10,073 | 18,053 | 19,915 |
| Gross Profit | 13,262 | 16,736 | 29,031 | 33,682 |
| Selling Expense | 3,503 | 4,300 | 8,054 | 8,810 |
| General and Administrative Expense | 3,852 | 6,140 | 8,105 | 11,644 |
| Engineering Expense | 1,021 | 1,152 | 2,141 | 2,493 |
| Operating Profit | 4,886 | 5,144 | 10,731 | 10,735 |
| Interest Income (Expense) | (97) | 236 | (52) | 456 |
| Other Income (Expense) | (23) | (33) | (131) | 5 |
| Income Before Income Taxes | 4,766 | 5,347 | 10,548 | 11,196 |
| Income Tax Expense | 1,196 | 1,325 | 2,612 | 2,743 |
| Net Income | 3,570 | 4,022 | 7,936 | 8,453 |
| Less: Net (Income) Loss attributable to the Noncontrolling Interest | 1 | (39) | (21) | (88) |
| Net Income attributable to Omega Flex, Inc. | $ 3,571 | $ 3,983 | $ 7,915 | $ 8,365 |
| Basic and Diluted Earnings per Common Share | $ 0.35 | $ 0.39 | $ 0.78 | $ 0.83 |
| Cash Dividends Declared per Common Share | $ 0.28 | $ 0.52 | $ 0.56 | $ 0.52 |
| Basic and Diluted Weighted Average Shares Outstanding | 10,094,322 | 10,092,124 | 10,094,322 | 10,091,973 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

**OMEGA FLEX, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**
**(Amounts in Thousands)**

| | For the three months ended June 30, | | For the six months ended June 30, | |
|---|---|---|---|---|
| | **2020** | **2019** | **2020** | **2019** |
| | | (Unaudited) | | |
| Net Income | $ 3,570 | $ 4,022 | $ 7,936 | $ 8,453 |
| Other Comprehensive Income (Loss): | | | | |
| Foreign Currency Translation Adjustment | (21) | (143) | (197) | (55) |
| Other Comprehensive Income (Loss) | (21) | (143) | (197) | (55) |
| Comprehensive Income | 3,549 | 3,879 | 7,739 | 8,398 |
| Less: Comprehensive (Income) Loss Attributable to the Noncontrolling Interest | 4 | (30) | (6) | (85) |
| Total Comprehensive Income | $ 3,553 | $ 3,849 | $ 7,733 | $ 8,313 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

**OMEGA FLEX, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**
**(Amounts in Thousands, Except Share Amounts)**

**For the three months ended June 30, 2020**

| | Common Stock Outstanding | Common Stock | Treasury Stock | Paid In Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Noncontrolling Interest | Shareholders' Equity |
|---|---|---|---|---|---|---|---|---|
| | | | | | (unaudited) | | | |
| **April 1, 2020** | 10,094,322 | $ 102 | ($ 1) | $ 11,025 | $ 28,683 | ( $1,073) | $ 204 | $ 38,940 |
| Net Income | | | | | 3,571 | | (1) | 3,570 |
| Cumulative Translation Adjustment | | | | | | (18) | (3) | (21) |
| Dividends Declared | | | | | (2,827) | | | (2,827) |
| **June 30, 2020** | 10,094,322 | $ 102 | ($ 1) | $ 11,025 | $ 29,427 | ($ 1,091) | $ 200 | $ 39,662 |

**For the three months ended June 30, 2019**

| | Common Stock Outstanding | Common Stock | Treasury Stock | Paid In Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Noncontrolling Interest | Shareholders' Equity |
|---|---|---|---|---|---|---|---|---|
| | | | | | (unaudited) | | | |
| **April 1, 2019** | 10,091,822 | $ 102 | ($ 1) | $ 10,808 | $ 60,492 | ($ 868) | $ 307 | $ 70,840 |
| Net Income | | | | | 3,983 | | 39 | 4,022 |
| Cumulative Translation Adjustment | | | | | | (134) | (9) | (143) |
| Shares Reissued From Treasury Pursuant To Restricted Stock Unit Awards | 2,500 | | | 217 | | | | 217 |
| Dividends Declared | | | | | (5,248) | | | (5,248) |
| **June 30, 2019** | 10,094,322 | $ 102 | ($ 1) | $ 11,025 | $ 59,227 | ($ 1,002) | $ 337 | $ 69,688 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

**OMEGA FLEX, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**
**(Amounts in Thousands, Except Share Amounts)**

**For the six months ended June 30, 2020**

| | Common Stock Outstanding | Common Stock | Treasury Stock | Paid In Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Noncontrolling Interest | Shareholders' Equity |
|---|---|---|---|---|---|---|---|---|
| | | | | | (unaudited) | | | |
| **January 1, 2020** | 10,094,322 | $ 102 | ($ 1) | $ 11,025 | $ 27,165 | ($ 909) | $ 194 | $ 37,576 |
| Net Income | | | | | 7,915 | | 21 | 7,936 |
| Cumulative Translation Adjustment | | | | | | (182) | (15) | (197) |
| Dividends Declared | | | | | (5,653) | | | (5,653) |
| **June 30, 2020** | 10,094,322 | $ 102 | ($ 1) | $ 11,025 | $ 29,427 | ($ 1,091) | $ 200 | $ 39,662 |

**For the six months ended June 30, 2019**

| | Common Stock Outstanding | Common Stock | Treasury Stock | Paid In Capital | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Noncontrolling Interest | Shareholders' Equity |
|---|---|---|---|---|---|---|---|---|
| | | | | | (unaudited) | | | |
| **January 1, 2019** | 10,091,822 | $ 102 | ($ 1) | $ 10,808 | $ 56,110 | ($ 950) | $ 252 | $ 66,321 |
| Net Income | | | | | 8,365 | | 88 | 8,453 |
| Cumulative Translation Adjustment | | | | | | (52) | (3) | (55) |
| Shares Reissued From Treasury Pursuant To Restricted Stock Unit Awards | 2,500 | | | 217 | | | | 217 |
| Dividends Declared | | | | | (5,248) | | | (5,248) |
| **June 30, 2019** | 10,094,322 | $ 102 | ($ 1) | $ 11,025 | $ 59,227 | ($ 1,002) | $ 337 | $ 69,688 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

**OMEGA FLEX, INC.**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(Amounts in Thousands)**

| | For the six months ended June 30, | |
|---|---|---|
| | **2020** | **2019** |
| | (unaudited) | |
| Cash Flows from Operating Activities: | | |
| Net Income | $7,936 | $8,453 |
| Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities: | | |
| Non-Cash Compensation | 142 | 1,145 |
| Depreciation and Amortization | 421 | 301 |
| Provision for Losses on Accounts Receivable, net of write-offs and recoveries | (531) | (42) |
| Deferred Taxes | (145) | (355) |
| Provision for Inventory Reserves | (55) | (29) |
| Changes in Assets and Liabilities: | | |
| Accounts Receivable | 3,371 | (199) |
| Inventories | (63) | (1,388) |
| Right-Of-Use Assets | 163 | (778) |
| Other Assets | 1,092 | 919 |
| Accounts Payable | (206) | (1,043) |
| Accrued Compensation | (2,258) | (3,019) |
| Accrued Commissions and Sales Incentives | (1,605) | (861) |
| Lease Liabilities | (166) | 796 |
| Other Liabilities | 1,207 | 1,179 |
| Net Cash Provided by Operating Activities | 9,303 | 5,079 |
| Cash Flows from Investing Activities: | | |
| Purchase of Investments | --- | (22,954) |
| Net Proceeds from Sale of Investments | --- | 15,000 |
| Capital Expenditures | (187) | (722) |
| Net Cash Used in Investing Activities | (187) | (8,676) |
| Cash Flows from Financing Activities: | | |
| Dividends Paid | (5,653) | (4,844) |
| Net Cash Used in Financing Activities | (5,653) | (4,844) |
| Net Increase (Decrease) in Cash and Cash Equivalents | 3,463 | (8,441) |
| Translation effect on cash | (74) | (31) |
| Cash and Cash Equivalents – Beginning of Period | 16,098 | 32,392 |
| Cash and Cash Equivalents – End of Period | $19,487 | $23,920 |
| Supplemental Disclosure of Cash Flow Information: | | |
| Cash paid for Income Taxes | $ 458 | $2,404 |
| Cash paid for Interest | $ 112 | $ --- |
| Declared Dividends | $ 5,653 | $5,248 |

See Accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

**OMEGA FLEX, INC.**

**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

## 1. BASIS OF PRESENTATION AND DESCRIPTION OF BUSINESS

### Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Omega Flex, Inc. (Omega) and its subsidiaries (collectively the "Company"). The Company's unaudited condensed consolidated financial statements for the quarter ended June 30, 2020 have been prepared in accordance with accounting principles generally accepted in the United States (GAAP), and with the instructions of Form 10-Q and Article 10 of Regulation S-X. Certain information and note disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to those rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading. It is suggested that these condensed consolidated financial statements be read in conjunction with the financial statements and the notes thereto included in the Company's latest shareholders' annual report (Form 10-K). All material inter-company accounts and transactions have been eliminated in consolidation. It is Management's opinion that all adjustments necessary for a fair statement of the results for the interim periods have been made, and that all adjustments are of a normal recurring nature or a description is provided for any adjustments that are not of a normal recurring nature.

### Description of Business

The Company's business is controlled as a single operating segment that consists of the manufacture and sale of flexible metal hose (also described as corrugated tubing), as well as the sale of the Company's related proprietary fittings and a vast array of accessories.

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

The Company manufactures flexible metal hose at its facilities in Exton, Pennsylvania and Houston, Texas, in the United States, and in Banbury, Oxfordshire in the United Kingdom, and sells its products through distributors, wholesalers and to original equipment manufacturers ("OEMs") throughout North America, and in certain European markets.

**COVID-19 Pandemic**

The emergence of the coronavirus (COVID-19) pandemic in the United States (U.S.), United Kingdom (U.K.) and around the world, presents significant risks to the Company, not all of which the Company is able to fully evaluate or articulate at the current time. This has caused and is continuing to cause business slowdowns and shutdowns and turmoil in the financial markets both in the U.S. and abroad. The Company is monitoring the impact of the COVID-19 pandemic on its business, including how it has impacted and will impact the Company's employees, customers, suppliers and distribution channels. The COVID-19 pandemic, as well as the quarantines and other governmental and non-governmental restrictions which have been imposed throughout the world in an effort to contain or mitigate the spread of the coronavirus, has created significant volatility, uncertainty and economic disruption which has begun to and is expected to continue to significantly affect the Company's business. The extent of the impact of the COVID-19 pandemic on the Company's business is highly uncertain and difficult to predict, as information is rapidly evolving with respect to the duration and severity of the COVID-19 pandemic. Currently, the Company cannot reasonably estimate the duration and severity of the COVID-19 pandemic or its overall impact on the Company's business.

## 2. SIGNIFICANT ACCOUNTING POLICIES

**Use of Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. The most significant estimates and assumptions relate to revenue recognition and related sales incentives, accounts receivable allowances, investment valuations, inventory valuations, goodwill valuation, product liability reserve, stock-based compensation valuations and accounting for income taxes. Actual amounts could differ significantly from these estimates.

**Revenue Recognition**

According to Accounting Standards Update 2014-09, *Revenue from Contracts with Customers (Topic 606)*, the Company recognizes revenue in a manner to depict the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services.

The principle of Topic 606 is achieved through applying the following five-step approach:

- *Identification of the contract, or contracts, with a customer* — a contract with a customer exists when the Company enters into an enforceable contract with a customer, typically a purchase order initiated by the customer, that defines each party's rights regarding the goods to be transferred and identifies the payment terms related to these goods.

- *Identification of the performance obligations in the contract* — performance obligations promised in a contract are identified based on the goods that will be transferred to the customer that are distinct, whereby the customer can benefit from the goods on their own or together with other resources that are readily available from third parties or from us. Persuasive evidence of an arrangement for the sale of product must exist. The Company ships product in accordance with the purchase order and standard terms as reflected within the Company's order acknowledgments and sales invoices.

- *Determination of the transaction price* —the transaction price is determined based on the consideration to which the Company will be entitled in exchange for transferring goods to the customer. This would be the agreed upon quantity and price per product type in accordance with the customer purchase order, which is aligned with the Company's internally approved pricing guidelines.

- *Allocation of the transaction price to the performance obligations in the contract* — if the contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. This applies to the Company as there is only one performance obligation to ship the goods.

- *Recognition of revenue when, or as, the Company satisfies a performance obligation* — the Company satisfies performance obligations at a point in time when control of the goods transfers to the customer. Determining the point in time when control transfers requires judgment. Indicators considered in determining whether the customer has obtained control of a good include:
    - The Company has a present right to payment
    - The customer has legal title to the goods
    - The Company has transferred physical possession of the goods
    - The customer has the significant risks and rewards of ownership of the goods
    - The customer has accepted the goods

  It is important to note that the indicators are not a set of conditions that must be met before the Company can conclude that control of the goods has transferred to the customer. The indicators are a list of factors that are often present if a customer has control of the goods.

  The Company has typical, unmodified FOB shipping point terms. As the seller, the Company can determine that the shipped goods meet the agreed-upon specifications in the contract or customer purchase order (e.g. items, quantities, and prices) with the buyer, so customer acceptance would be deemed a formality, as noted in ASC 606-10-55-86. As a result, the Company has a legal right to payment upon shipment of the goods.

  Based upon the above, the Company has concluded that transfer of control substantively transfers to the customer upon shipment.

Other considerations of Topic 606 include the following:

- *Contract Costs* - costs to obtain a contract (e.g. customer purchase order) include sales commissions. Under Topic 606, these costs may be expensed as incurred for contracts with a duration of one year or less. The majority of the Company's customer purchase orders are fulfilled (e.g. goods are shipped) within two days of receipt.

- *Warranties* - the Company does not offer customers to purchase a warranty separately. Therefore, there is not a separate performance obligation. The Company does account for warranties as a cost accrual and the warranties do not include any additional distinct services other than the assurance that the goods comply with agreed-upon specifications. There is no impact of warranties under Topic 606 upon the financial reporting of the Company.

- *Returned Goods* - from time to time, the Company provides authorization to customers to return goods. If deemed to be material, the Company would record a "right of return" asset for the cost of the returned goods which would reduce cost of sales.

- *Volume Rebates (Promotional Incentives)* - volume rebates are variable (dependent upon the volume of goods purchased by our eligible customers) and, under Topic 606, must be estimated and recognized as a reduction of revenue as performance obligations are satisfied (e.g. upon shipment of goods). Also, under Topic 606, to ensure that revenue recognized would not be probable of a significant reversal, the four following factors are considered:

  - The amount of consideration is highly susceptible to factors outside the Company's influence.
  - The uncertainty about the amount of consideration is not expected to be resolved for a long period of time.
  - The Company's experience with similar types of contracts is limited.
  - The contract has a large number and broad range of possible consideration amounts.

  If it was concluded that the above factors were in place for the Company, it would support the probability of a significant reversal of revenue. However, as none of the four factors apply to the Company, promotional incentives are recorded as a reduction of revenue based upon estimates of the eligible products expected to be sold.

Regarding disaggregated revenue disclosures, as previously noted, the Company's business is controlled as a single operating segment that consists of the manufacture and sale of flexible metal hose. Most of the Company's transactions are very similar in nature, contract, terms, timing, and transfer of control of goods. As indicated within Note 2, under the caption "Significant Concentration", the majority of the Company's sales were geographically contained within North America, with the remainder scattered internationally. All performance assessments and resource allocations are generally based upon the review of the results of the Company as a whole.

## **Cash Equivalents**

The Company considers all highly liquid investments with an original maturity of 90 days or less at the time of purchase to be cash equivalents. Cash equivalents include investments in an institutional money market fund, which invests in U.S. Treasury bills, notes and bonds, and/or repurchase agreements, backed by such obligations. Carrying value approximates fair value. Cash and cash equivalents are deposited at various area banks, which at times may exceed federally insured limits. The Company monitors the viability of the banking institutions carrying its assets on a regular basis, and has the ability to transfer cash to various institutions during times of risk. The Company has not experienced any losses related to these cash balances, and believes its credit risk to be minimal.

## **Accounts Receivable and Provision for Credit Losses**

All accounts receivables are stated at amortized cost, net of allowances for credit losses, and adjusted for any write-offs. The Company maintains allowances for credit losses, which represent an estimate of expected losses over the remaining contractual life of its receivables considering current market conditions and estimates for supportable forecasts when appropriate. The estimate is a result of the Company’s ongoing assessments and evaluations of collectability, historical loss experience, and future expectations in estimating credit losses in its receivable portfolio. For accounts receivables, the Company uses historical loss experience rates and applies them to a related aging analysis while also considering customer and/or economic risk where appropriate. Determination of the proper amount of allowances requires management to exercise judgment about the timing, frequency and severity of credit losses that could materially affect the provision for credit losses and, as a result, net earnings. The allowances consider numerous quantitative and qualitative factors that include receivable type, historical loss experience, delinquency trends, collection experience, current economic conditions, estimates for supportable forecasts, when appropriate, and credit risk characteristics.

The reserve for credit losses, which include future credits, discounts, and doubtful accounts, was $887,000 and $1,433,000 as of June 30, 2020 and December 31, 2019, respectively.

## **Investments**

The Company invests excess funds in liquid interest earning instruments including U.S. Treasury bills and bank time deposits, with maturities typically of one year or less. These investments are stated at fair value, which approximates amortized cost, and are classified as available-for-sale in accordance with ASC 320, *Investments – Debt and Equity Securities*. The Company did not have any investments as of June 30, 2020 and December 31, 2019, respectively.

## **Inventories**

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

**Property and Equipment**

Property and equipment are initially recorded at cost. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets or, for leasehold improvements, the life of the lease, if shorter. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in other income or expense for the period. The cost of maintenance and repairs is expensed as incurred; significant improvements are capitalized.

**Goodwill**

In accordance with Financial Accounting Standards Board ("FASB") ASC Topic 350, *Intangibles – Goodwill and Other*, the Company performed an annual impairment test as of December 31, 2019. This analysis did not indicate any impairment of goodwill.

However, the duration and severity of the COVID-19 pandemic could result in future goodwill impairment charges. While we have concluded that a triggering event did not occur during the six months ended June 30, 2020, a prolonged pandemic could impact the Company's results of operations in a manner significant enough to trigger an interim impairment test.

**Stock-Based Compensation Plans**

In 2006, the Company adopted a Phantom Stock Plan (the "Plan"), which allows the Company to grant phantom stock units ("Units") to certain key employees, officers or directors. The Units each represent a contractual right to payment of compensation in the future based upon the market value of the Company's common stock. The Units follow a vesting schedule of three years from the grant date, and are then paid upon maturity. In accordance with FASB ASC Topic 718, *Compensation - Stock Compensation* ("Topic 718"), the Company uses the Black-Scholes option pricing model as its method for determining the fair value of the Units and are accordingly recorded as liabilities. Additionally, the liabilities for the Units are adjusted to market value over time from the grant dates to the related maturity dates. Further details of the Plan are provided in Note 6.

**Product Liability Reserves**

Product liability reserves represent the estimated unpaid amounts under the Company's insurance policies with respect to existing claims. The Company uses the most current available data to estimate claims. As explained more fully under Note 5, Commitments and Contingencies, for various product liability claims covered under the Company's general liability insurance policies, the Company must pay certain defense and settlement costs within its deductible or self-insured retention limits, ranging primarily from $25,000 to $1,000,000 per claim, depending on the terms of the policy in the applicable policy year, up to an aggregate amount. The Company is vigorously defending against all known claims.

## **Leases**

Effective January 1, 2019, the Company adopted the requirements of FASB ASU 2016-02, *Leases* (Topic 842) which defines a lease as any contract that conveys the right to use a specific asset for a period of time in exchange for consideration. Leases are classified as a finance lease, formerly called a capital lease, if any of the following criteria are met:

1. The lease transfers ownership of the underlying asset to the lessee by the end of the lease term.
2. The lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise.
3. The lease term is for the major part of the remaining economic life of the underlying asset.
4. The present value of the sum of lease payments and any residual value guaranteed by the lessee equals or exceeds substantially all of the fair value of the underlying asset.
5. The underlying asset is of such a specialized nature that it is expected to have no alternative use to the lessor at the end of the lease term.

For any leases that do not meet the criteria identified above for finance leases, the Company treats such leases as operating leases. As of June 30, 2020, each of the Company's leases are classified as operating leases.

Both finance and operating leases are reflected on the balance sheet as lease or "right-of-use" assets and lease liabilities.

There are some exceptions, which the Company has elected in its accounting policies. For leases with terms of twelve months or less, or below the Company's general capitalization policy threshold, the Company has elected an accounting policy to not recognize lease assets and lease liabilities for all asset classes. The Company recognizes lease expense for such leases generally on a straight-line basis over the lease term.

The Company determines if a contract is a lease at the inception of the arrangement. The Company reviews all options to extend, terminate, or purchase its right-of-use assets at the inception of the lease and accounts for these options when they are reasonably certain to be exercised. Certain leases contain non-lease components, such as common area maintenance, which are generally accounted for separately. In general, the Company will assess if non-lease components are fixed and determinable, or variable, when determining if the component should be included in the lease liability. For purposes of calculating the present value of the lease obligations, the Company utilizes the implicit interest rate within the lease agreement when known and/or determinable, and otherwise utilizes its incremental borrowing rate at the time of the lease agreement.

As permitted under ASU 2018-11, the Company elected the optional transition method to adopt the new leases standard. Under this new transition method, the Company initially applied the new leases standard at the adoption date of January 1, 2019 and would have recognized a cumulative-effect adjustment, if appropriate, to the opening balance of retained earnings in the period of adoption. No cumulative-effect adjustment was recognized.

The impact of the adoption of this new standard resulted in an increase to the Company's operating lease assets and liabilities on January 1, 2019 of approximately $800,000. The implementation did not have a material impact on our consolidated statements of income and statements of cash flows.

**Fair Value of Financial and Nonfinancial Instruments**

The Company measures financial instruments in accordance with FASB ASC Topic 820, *Fair Value Measurements and Disclosures*. The accounting standard defines fair value, establishes a framework for measuring fair value under GAAP, and enhances disclosures about fair value measurements. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard creates a fair value hierarchy which prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as follows: Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities; Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and Level 3 inputs are unobservable inputs that reflect the Company's own assumptions about the assumptions market participants would use in pricing the asset or liability. The Company relies upon Level 1 inputs in determining the fair value of investments and the fair value of the Company's reporting unit in its annual impairment test as described in the FASB ASC Topic 350, *Intangibles - Goodwill and Other*.

**Earnings per Common Share**

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

**Currency Translation**

Assets and liabilities denominated in foreign currencies, most of which relate to the Company's United Kingdom subsidiary whose functional currency is British pound sterling, are translated into U.S. dollars at exchange rates prevailing on the balance sheet dates. The statements of income are translated into U.S. dollars at average exchange rates for the period. Adjustments resulting from the translation of financial statements are excluded from the determination of income and are accumulated in a separate component of shareholders' equity. Exchange gains and losses resulting from foreign currency transactions are included in the statements of income (other expense) in the period in which they occur.

**Income Taxes**

The Company accounts for tax liabilities in accordance with the FASB ASC Topic 740, Income Taxes. Under this method the Company recorded tax expense, related deferred taxes and tax benefits, and uncertainties in tax positions.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities from a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided for deferred tax assets if it is more likely than not that these items will either expire before the Company is able to realize the benefit, or that future deductibility is uncertain.

The FASB ASC Topic 740, Income Taxes, clarifies the criteria that an individual tax position must satisfy for some or all of the benefits of that position to be recognized in a company's financial statements. This guidance prescribes a recognition threshold of more-likely than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for those tax positions to be recognized in the financial statements.

The Company follows the provisions of ASC 740-10 relative to accounting for uncertainties in tax positions. These provisions provide guidance on the recognition, de-recognition and measurement of potential tax benefits associated with tax positions.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security (CARES) Act was signed into law making several changes to the Internal Revenue Code. The changes include, but are not limited to: increasing the limitation on the amount of deductible interest expense, allowing companies to carryback certain net operating losses, and increasing the amount of net operating loss carryforwards that corporations can use to offset taxable income. The tax law changes in the Act have not had an effect on the Company's income tax provision for the three and six months ended June 30, 2020.

**Other Comprehensive Income**

For the three and six months ended June 30, 2020 and 2019, respectively, the components of other comprehensive income consisted solely of foreign currency translation adjustments.

**Significant Concentration**

The Company has one significant customer which represented more than 10% of the Company's Accounts Receivable at June 30, 2020 and December 31, 2019. That same customer represented more than 10% of the Company's total Net Sales for the three and six months ended June 30, 2020 and 2019. Geographically, the Company has a significant amount of sales in the United States versus internationally. These concentrations are consistent with those discussed in detail in the Company's December 31, 2019 Form 10-K.

**Subsequent Events**

The Company evaluates all events or transactions through the date of the related filing that may have a material impact on its condensed consolidated financial statements. Refer to Note 10 of the condensed consolidated financial statements.

**Recent Accounting Pronouncements**

In January 2017, the FASB amended ASC Topic 350, *Intangibles – Goodwill and Other* (issued under ASU 2017-04, "Simplifying the Test for Goodwill Impairment"). This amendment simplifies the test for goodwill impairment by only requiring an entity to perform an annual or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and recognizes an impairment charge for the amount that the carrying amount exceeds the reporting unit's fair value. Any loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The amendment required adoption on January 1, 2020. In compliance, the Company adopted ASU 2017-04 as required during the first quarter of 2020 and determined that there was no material impact on its condensed consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 replaced the incurred loss impairment methodology under current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. ASU 2016-13 requires use of a forward-looking expected credit loss model for accounts receivables, loans, and other financial instruments. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, with early adoption permitted. Adoption of the standard requires using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date to align existing credit loss methodology with the new standard. In November 2019, the FASB issued ASU 2019-11, Codification Improvements to Topic 326, Financial Instruments—Credit Losses. ASU 2019-11 requires entities that did not adopt the amendments in ASU 2016-13 as of November 2019 to adopt ASU 2019-11. This ASU contains the same effective dates and transition requirements as ASU 2016-13. We adopted ASU 2016-13 and ASU 2019-11 effective January 1, 2020. The impact of adoption of these standards on our condensed consolidated financial statements was not material.

## 3. INVENTORIES

Inventories, net of reserves of $288,000 and $355,000 at June 30, 2020 and December 31, 2019, respectively, consisted of the following:

| | June 30, 2020 | December 31, 2019 |
|---|---|---|
| | (dollars in thousands) | |
| Finished Goods | $5,834 | $5,409 |
| Raw Materials | 5,249 | 5,669 |
| Inventories - Net | $11,083 | $11,078 |

## 4. LINE OF CREDIT AND OTHER BORROWINGS

On December 1, 2017, the Company agreed to a new Amended and Restated Revolving Line of Credit Note and Third Amendment to the Loan Agreement with Santander Bank, N.A.

(the “Bank”). The Company established a line of credit facility in the maximum amount of $15,000,000, maturing on December 1, 2022, with funds available for working capital purposes and other cash needs. The loan is unsecured. The loan agreement provides for the payment of any borrowings under the agreement at an interest rate range of either LIBOR plus 0.75% to plus 1.75% (for borrowings with a fixed term of 30, 60, or 90 days), or, Prime Rate up to Prime Rate plus 0.50% (for borrowings with no fixed term other than the December 1, 2022 maturity date), depending upon the Company’s then existing financial ratios. Currently, the Company’s ratio would allow for the most favorable rate under the agreement’s range, which would be a rate of 0.91%. The Company is also required to pay on a quarterly basis an unused facility fee of 10 basis points of the average unused balance of the note. The Company may terminate the line at any time during the five-year term, as long as there are no amounts outstanding.

During the quarter ending June 30, 2020, in an effort to ensure liquidity and secure all available resources during the COVID-19 crisis, the Company borrowed the full amount of its capacity on the line of $15,000,000 at the prime rate of 3.50% and was repaid in full prior to the end of the quarter. As of December 31, 2019, the Company had no outstanding borrowings on its line of credit.

The Company was in compliance with all debt covenants as of June 30, 2020 and December 31, 2019.

The Coronavirus Aid, Relief, and Economic Security Act ("CARES Act") was enacted on March 27, 2020 in the United States. On April 7, 2020, the Company received a loan from the U.S. Small Business Administration (“SBA”) to fund the Company’s request for a loan under the SBA’s Paycheck Protection Program (“PPP” and “PPP Loan”) created as part of the recently enacted CARES Act administered by the SBA. In connection with the PPP Loan, the Company entered into a promissory note filed as Exhibit 10.2 attached to Form 10-Q for the quarter ending March 31, 2020. Pursuant to the terms of the PPP Loan, the Company received total proceeds of $2,453,000 from the Bank. After the issuance of the PPP Loan, the U.S. Treasury Department issued new guidance on the PPP program, and advised that publicly traded companies that had access to other sources of financing may not be appropriate candidates for the PPP Loans, and provided a grace period until May 7, 2020 for such companies to repay the previously issued PPP Loans. Accordingly, in light of this guidance, the Company repaid the PPP Loan by May 7, 2020.

## 5. COMMITMENTS AND CONTINGENCIES

**Commitments:**

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

The Company has salary continuation agreements with current and/or past employees. These agreements provide for monthly payments to each of the employees or their designated beneficiary upon the employee's retirement or death. The payment benefits range from $1,000 per month to $3,000 per month with the term of such payments limited to 15 years after the employee's retirement. The agreements also provide for survivorship benefits if the employee dies before attaining age 65, and severance payments if the employee is terminated without cause; the amount of which is dependent on the length of company service at the date of termination. The net present value of the retirement payments associated with these agreements is $491,000 at June 30, 2020, of which $479,000 is included in Other Long Term Liabilities, and the remaining current portion of $12,000 is included in Other Liabilities, associated with a retired employee who is now receiving benefit payments. The December 31, 2019 liability of $492,000 had $480,000 reported in Other Long Term Liabilities, and a current portion of $12,000 in Other Liabilities.

The Company has obtained and is the beneficiary of life insurance policies with respect to current and/or past employees. The cash surrender value of such policies (included in Other Long Term Assets) amounts to $1,441,000 at June 30, 2020 and $1,417,000 at December 31, 2019.

In addition to the above, the Company has other contractual employment and or change of control agreements in place with key employees, as previously disclosed and noted in the Exhibit Index to the Company's December 31, 2019 Form 10-K. There are no current payment obligations related to these arrangements, and any future obligations are currently indeterminable due to the variable nature and timing of possible events required to incur such obligations.

As disclosed in detail in Note 7, Leases, the Company has several lease obligations in place that will be paid out over time.

Lastly, as provided in Item 7 of the Company's December 31, 2019 Form 10-K, under the "Tabular Disclosure of Contractual Obligations and Off-Balance Sheet Arrangements", the Company has numerous purchase obligations in place for the forthcoming year, largely related to the Company's core material inventory components.

**Contingencies:**

In the ordinary and normal conduct of the Company's business, it is subject to periodic lawsuits, investigations and claims (collectively, the "Claims"). Most of the Claims, including a putative class-action claim, relate to potential lightning damage to our flexible gas piping products, which impact legal and product liability related expenses. The Company does not believe the Claims have legal merit, and therefore has commenced a vigorous defense in response to the Claims. It is possible that the Company may incur increased litigation costs in the future due to a variety of factors, including a higher number of Claims, higher legal costs, and higher insurance deductibles or retentions.

In June 2017, a putative class action case was re-filed against the Company and other parties in Missouri state court after the predecessor case was dismissed without prejudice by the federal court. The Company successfully removed the case to federal court and is currently vigorously defending the case.

The Company was made aware of a potential legal liability regarding a legal dispute in the United Kingdom, in which the Company's subsidiary, Omega Flex Limited ("OFL"), was the claimant. After reviewing currently available information, there are a range of possible outcomes; (1) from British Standards Institution ("BSI"), the defendant, paying OFL a portion of its legal costs incurred in the action, (2) to each side bearing its own costs, or (3) OFL paying a portion of BSI's legal costs. The potential amount of loss in the last outcome (paying BSI's legal costs) is estimated to be between $200,000 and $500,000. No amounts have been recorded for the potential liability at this time due to the uncertainty of the ultimate outcome, and the potential loss is not deemed probable.

The Company has in place commercial general liability insurance policies that cover most Claims, which are subject to deductibles or retentions, ranging primarily from $25,000 to $1,000,000 per claim (depending on the terms of the policy and the applicable policy year), up to an aggregate amount. Litigation is subject to many uncertainties and management is unable to predict the outcome of the pending suits and claims. The potential liability for a given claim could range from zero to a maximum of $1,000,000, depending upon the circumstances, and insurance deductible or retention in place for the respective claim year. The aggregate maximum exposure for all current open Claims, excluding the Missouri class action case, as of June 30, 2020 is estimated to not exceed approximately $5,800,000, which represents the potential costs that may be incurred over time for the Claims within the applicable insurance policy deductibles or retentions. From time to time, depending upon the nature of a particular case, the Company may decide to spend in excess of a deductible or retention to enable more discretion regarding the defense, although this is not common. It is possible that the results of operations or liquidity of the Company, as well as the Company's ability to procure reasonably priced insurance, could be adversely affected by the pending litigation, potentially materially. The Company is currently unable to estimate the ultimate liability, if any, that may result from the pending litigation, or potential litigation from future claims or claims that have not yet come to our attention, and accordingly, the liability in the consolidated financial statements primarily represents an accrual for legal costs for services previously rendered, and outstanding or anticipated settlements for Claims. The liabilities recorded on the Company's books at June 30, 2020 and December 31, 2019 were $150,000 and $215,000, respectively, and are included in Other Liabilities.

## 6. STOCK BASED PLANS

### Phantom Stock Plan

***Plan Description.*** On April 1, 2006, the Company adopted the Omega Flex, Inc. 2006 Phantom Stock Plan (the "Plan"). The Plan authorizes the grant of up to one million units of phantom stock to employees, officers or directors of the Company. The phantom stock units ("Units") each represent a contractual right to payment of compensation in the future based on the market value of the Company's common stock. The Units are not shares of the Company's common stock, and a recipient of the Units does not receive any of the following:

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

The Units are granted to participants upon the recommendation of the Company's CEO, and the approval of the Compensation Committee. Each of the Units that are granted to a participant will be initially valued by the Compensation Committee, at an amount equal to the closing price of the Company's common stock on the grant date, but are recorded at fair value using the Black-Sholes method as described below. The Units follow a vesting schedule, with a maximum vesting of three years after the grant date. Upon vesting, the Units represent a contractual right of payment for the value of the Unit and therefore are stated as liabilities in accordance with Topic 718. The Units will be paid on their maturity date, one year after all of the Units granted in a particular award have fully vested, unless an acceptable event occurs under the terms of the Plan prior to one year, which would allow for earlier payment. The amount to be paid to the participant on the maturity date is dependent on the type of Unit granted to the participant.

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

On December 9, 2009, the Board of Directors authorized an amendment to the Plan to pay an amount equal to the value of any cash or stock dividend declared by the Company on its common stock to be accrued to the phantom stock units outstanding as of the record date of the common stock dividend. The dividend equivalent will be paid at the same time the underlying phantom stock units are paid to the participant.

In certain circumstances, the Units may be immediately vested upon the participant's death or disability. All Units granted to a participant are forfeited if the participant is terminated from his relationship with the Company or its subsidiary for "cause," which is defined under the Plan. If a participant's employment or relationship with the Company is terminated for reasons other than for "cause," then any vested Units will be paid to the participant upon termination. However, Units granted to certain "specified employees" as defined in Section 409A of the Internal Revenue Code will be paid approximately 181 days after termination.

***Grants of Phantom Stock Units.*** As of December 31, 2019, the Company had 15,493 unvested units outstanding, all of which were granted at *Full Value*. On February 28, 2020, the Company granted an additional 4,875 *Full Value* Units with a fair value of $74.52 per unit on grant date, using historical volatility. In February 2020, the Company paid $968,000 for the 10,460 fully vested and matured units that were granted during 2016, including their respective earned dividend values. As of June 30, 2020, the Company had 13,618 unvested units outstanding.

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

Topic 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates in order to derive the Company's best estimate of awards ultimately to vest.

Forfeitures represent only the unvested portion of a surrendered Unit and are typically estimated based on historical experience. Based on an analysis of the Company's historical data, which has limited experience related to any stock-based plan forfeitures, the Company applied a 0% forfeiture rate to Plan Units outstanding in determining its Plan Unit compensation expense as of June 30, 2020.

The total Phantom Stock related liability as of June 30, 2020 was $2,374,000 of which $1,179,000 is included in Other Liabilities, as it is expected to be paid within the next twelve months, and the balance of $1,195,000 is included in Other Long Term Liabilities. At December 31, 2019, the total Phantom Stock liability was $3,201,000, with $1,508,000 in Other Liabilities, and $1,693,000 included in Other Long Term Liabilities.

Related to the Phantom Stock Plan, in accordance with Topic 718, the Company recorded compensation expense of approximately $142,000 and $928,000 for the six months ended June 30, 2020 and 2019, respectively. Compensation expense for a given period largely depends upon fluctuations in the Company's stock price.

The following table summarizes information about the Company's nonvested phantom stock Units at June 30, 2020:

| | **Units** | **Weighted Average Grant Date Fair Value** |
|---|---|---|
| Number of Phantom Stock Unit Awards: | | |
| Nonvested at December 31, 2019 | 15,493 | $59.65 |
| Granted | 4,875 | $74.52 |
| Vested | (6,750) | $52.38 |
| Forfeited | --- | --- |
| Canceled | --- | --- |
| Nonvested at June 30, 2020 | 13,618 | $68.58 |
| Phantom Stock Unit Awards Expected to Vest | 13,618 | $68.58 |

The total unrecognized compensation costs calculated at June 30, 2020 are $1,078,000 which will be recognized through February of 2023. The Company will recognize the related expense over the weighted average period of 1.5 years.

## 7. LEASES

In the United States, the Company owns its two main operating facilities located in Exton, PA, which provide manufacturing, warehousing and distribution space. In addition to the owned facilities, the Company also has operations in other locations that are leased, as well as other leased assets.

With regards to leased facilities within the United States, the Company leases its corporate office space in Middletown, CT, with the lease term expiring in 2022. Additionally, the Company leases a warehousing and distribution center in Houston, Texas, which currently provides manufacturing, stocking and sales operations, with a 5-year lease term running through October 2024.

In the United Kingdom, the Company leases a facility in Banbury, England, which serves sales, warehousing and operational functions. The lease in Banbury has a 15-year term ending in June 2021.

In addition to property rentals, the Company also has lease agreements in place for various fleet vehicles and equipment with various lease terms.

In the June 30, 2020 condensed consolidated balance sheet, the Company has recorded right-of-use assets of $589,000, and a lease liability of $602,000, of which $311,000 is reported as a current liability. The respective weighted average remaining lease term and discount rate are approximately 2.52 years and 3.31%.

Future minimum lease payments under non-cancellable leases as of June 30, 2020, are as follows:

| **Twelve Months Ending June 30,** | **Operating Leases** (in thousands) | |
|---|---|---|
| 2021 | $ | 311 |
| 2022 | | 163 |
| 2023 | | 62 |
| 2024 | | 47 |
| 2025 | | 18 |
| Thereafter | | 1 |
| Total Minimum Lease Payments | $ | 602 |

A similar description of the lease obligations for the previous year is disclosed in the Company's December 31, 2019 Form 10-K.

Lease expense for the operating leases was approximately $74,000 and $149,000 for the three and six months ended June 30, 2020 and $75,000 and $150,000 for the three and six months ended June 30, 2019. Lease expense is allocated to each portion of the business generally based upon use, with the majority absorbed by manufacturing (cost of goods sold), and the remainder apportioned to selling, administrative and engineering.

## 8. SHAREHOLDERS' EQUITY

As of June 30, 2020 and December 31, 2019, the Company had authorized 20,000,000 common stock shares with par value of $0.01 per share. For both periods, the total number of outstanding shares was 10,094,322, shares held in Treasury was 59,311, and total shares issued was 10,153,633.

During 2020 and 2019, upon approval of the Board of Directors (the "Board") the Company has declared and paid regular quarterly dividends, as well as special dividends, as set forth in the following table:

| Dividend Declared | | Dividend Paid | |
|---|---|---|---|
| Date | Price Per Share | Date | Amount |
| June 24, 2020 | $0.28 | July 13, 2020* | $2,826,000 |
| March 31, 2020 | $0.28 | April 17, 2020* | $2,826,000 |
| December 16, 2019 *(S)* | $3.50 | December 30, 2019* | $35,330,000 |
| December 14, 2019 | $0.28 | January 3, 2020* | $2,826,000 |
| September 6, 2019 | $0.28 | October 2, 2019* | $2,826,000 |
| June 13, 2019 | $0.28 | July 2, 2019* | $2,826,000 |
| April 9, 2019 | $0.24 | April 29, 2019** | $2,422,000 |
| December 13, 2018 | $0.24 | January 3, 2019** | $2,422,000 |

The number of shares outstanding on the dividend payment date was *10,094,322 and **10,091,822.
*(S)* indicates special dividend

In addition to the above dividend amounts, there were dividends approved by the Company's foreign subsidiary during July and December of 2019, with the cash distribution to the noncontrolling interest of $137,000 and $65,000, respectively, paid during those respective months.

It should be noted that from time to time, the Board may elect to pay special dividends, in addition to or in lieu of the regular quarterly dividends, depending upon the financial condition of the Company. Special dividends are indicated in the above schedule as *(S)*.

The Board approved and granted a total of 2,500 restricted stock unit awards (the "Awards") to be allocated to the existing non-employee directors of the Company. The Awards were approved by the shareholders of the Company at the annual meeting on June 11, 2019, and distributed on June 20, 2019. A Form S-8 registration statement, and the restricted stock unit award agreements, were filed with the SEC on December 13, 2018 (2,000 units) and May 24, 2019 (500 units). The related director compensation cost of approximately $217,000 was recognized during June 2019.

On April 4, 2014, the Board authorized an extension of its stock repurchase program without expiration, up to a maximum amount of $1,000,000. The original program established in December 2007 authorized the purchase of up to $5,000,000 of its common stock. The purchases may be made from time-to-time in the open market or in privately negotiated transactions, depending on market and business conditions. The Board retained the right to cancel, extend, or expand the share buyback program, at any time and from time-to-time. Since inception, the Company has purchased a total of 61,811 shares for approximately $932,000, or approximately $15 per share, which were held as treasury shares. The Company has not made any stock repurchases since 2014; however, as stated above, there were 2,500 shares distributed from treasury to non-employee directors during June 2019.

## 9. RELATED PARTY TRANSACTIONS

From time to time the Company may have related party transactions ("RPTs"). In short, RPTs represent any transaction between the Company and any Company employee, director or officer, or any related entity, or relative, etc. The Company performs a review of transactions each year to determine if any RPTs exist, and if so, determines if the related parties act independently of each other in a fair transaction. Through this investigation the Company noted a limited number of RPTs which are disclosed hereto. Legal services were performed by a firm which formerly employed one member of the board. On occasion the Company shares a small amount of services with its former parent Mestek, Inc., mostly related to board meeting expenses. The Company is aware of transactions between a few service providers which employ individuals indirectly associated to Omega Flex employees. In all cases, these transactions have been determined to be independent transactions with no indication that they are influenced by the related relationships. During the first six months of 2020, the Company had both provided and subsequently collected $5,000 of note agreement assets with related parties. Other than as disclosed above, the Company is currently not aware of any RPTs between the Company and any of its current directors or officers outside the scope of their normal business functions or expected contractual duties.

## 10. SUBSEQUENT EVENTS

The Company evaluated all events or transactions that occurred through the date of this filing. During this period, no events other than as discussed above came to the Company's attention that would impact the condensed consolidated financial statements.

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

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

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

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

## OVERVIEW

The Company is a leading manufacturer of flexible metal hose (also described as corrugated tubing), and is currently engaged in a number of different markets, including construction, manufacturing, transportation, petrochemical, pharmaceutical, healthcare and other industries.

The Company’s business is managed as a single operating segment that consists of the manufacture and sale of flexible metal hose, as well as the sale of the Company’s related proprietary fittings and a vast array of accessories. The Company’s products are concentrated in residential and commercial construction, and general industrial markets, with a comprehensive portfolio of intellectual property and patents issued in various countries around the world. The Company’s primary product, flexible gas piping, is used for gas piping within residential and commercial buildings. Through its flexibility and ease of use, the Company’s TracPipe® and TracPipe® CounterStrike® flexible gas piping, along with its fittings distributed under the trademarks AutoSnap® and AutoFlare®, allows users to substantially cut the time required to install gas piping, as compared to traditional methods. The Company’s products are manufactured at its facilities in Exton, Pennsylvania and Houston, Texas in the United States, and in Banbury, Oxfordshire in the United Kingdom. Through the use of its broad network of independent outside sales organizations, such as sales representatives, the Company primarily sells its products to distributors, wholesalers and OEM’s, mostly throughout North America, and to a lesser extent in other global markets.

## COVID-19 PANDEMIC

The emergence and escalation of the coronavirus (COVID-19) in the United States (U.S.), United Kingdom (U.K.), and around the world presents significant risks to the Company, not all of which the Company is able to fully evaluate or quantify at the present time. While the effects of the COVID-19 pandemic did slightly affect the Company's financial results and business operations during the three months ended June 30, 2020, most of those negative effects were in the early period of the quarter, with sales progressively growing during the second quarter.

Sales from our TracPipe® and CounterStrike® flexible gas piping products were impacted by the deterioration in construction activity during April, which continued during May, albeit on a less pronounced trajectory, and then experienced a resurgence of activity during June 2020, most notably within the U.S., as sales and profitability during June 2020 exceeded June 2019. Sales of our MediTrac® flexible medical gas piping has increased strongly as demand for rapid deployment of medical gases in temporary or retro-fitted medical facilities were required to treat patients affected by the COVID-19 virus. Additionally, sales of our industrial products, particularly flexible hose assemblies have also been used in pharmaceutical applications. In combination, the Company has therefore managed to maintain a reasonable level of sales and profitability despite the obstacles presented by these turbulent times.

The Company has responded to the challenges of the COVID-19 pandemic by taking measures to protect its workforce and supply chain. The Company currently maintains the full use of its $15,000,000 line of credit facility with Santander Bank N.A., and has other banking resources as well to assure liquidity.

Due to the above circumstances and as described generally in this Form 10-Q, the Company's results of operations for the three and six months ended June 30, 2020 are not indicative of the results to be expected for the full year. Management cannot predict the full impact of the COVID-19 pandemic on the Company's operations. The ultimate extent of the effects of the COVID-19 pandemic on the Company is highly uncertain and will depend on future developments, and such effects could exist for an extended period of time.

## CHANGES IN FINANCIAL CONDITION

### For the period ended June 30, 2020 vs. December 31, 2019

The Company's cash balance of $19,487,000 at June 30, 2020, increased $3,389,000 (21.1%) from the $16,098,000 balance at December 31, 2019 mainly the result of income generated from operations during 2020, less dividends of $5,653,000 paid during the first six months of 2020. The condensed consolidated statement of cash flows is provided on page 8 which provides further details regarding changes in cash.

Accounts Receivable was $14,113,000 and $17,047,000 as of June 30, 2020 and December 31, 2019, respectively, decreasing $2,934,000 or 17.2%. This is mostly timing related, associated with greater cash collections resulting from higher sales during the fourth quarter of 2019 versus the second quarter of 2020. Sales were lower during the second quarter of 2020 largely as a result of the impacts of the COVID-19 pandemic.

Accrued Compensation was $2,337,000 at June 30, 2020, compared to $4,618,000 at December 31, 2019, decreasing $2,281,000 (49.4%). A significant portion of the liability that existed at the previous year end related to incentive compensation earned in 2019. As is customary, the liability was then paid during the first quarter of the following year, or 2020, thus diminishing the balance. The liability now represents amounts earned during the current year.

Accrued Commissions and Sales Incentives were $2,846,000 at June 30, 2020, compared to $4,461,000 at December 31, 2019, decreasing $1,615,000 (36.2%). A portion of the decrease relates to the lower level of sales during the second quarter of 2020, in comparison to the fourth quarter of 2019, and the resulting commissions and sales incentives that are earned. Additionally, a portion of the sales incentives have an annual component which accumulates during the year and are then paid during the first quarter of the following year.

Taxes Payable were $2,858,000 at June 30, 2020 and $423,000 at the end of 2019, reflecting an increase of $2,435,000 or 575.7%. The increase mainly relates to the timing of payments of U.S. federal and state corporate income taxes. During the current year the Internal Revenue Service extended the time to pay current and prior year corporate income taxes as a result of the COVID-19 pandemic. The majority of state taxing authorities followed the extensions of time allowed by the Internal Revenue Service.

## RESULTS OF OPERATIONS

### Three months ended June 30, 2020 vs. June 30, 2019

The Company reported comparative results from continuing operations for the three months ended June 30, 2020 and 2019 as follows:

| | Three months ended June 30, (in thousands) | | | |
|---|---|---|---|---|
| | **2020** | **2020** | **2019** | **2019** |
| | **($000)** | **%** | **($000)** | **%** |
| Net Sales | $21,818 | 100.0% | $26,809 | 100.0% |
| Gross Profit | $13,262 | 60.8% | $16,736 | 62.4% |
| Operating Profit | $ 4,886 | 22.4% | $ 5,144 | 19.2% |

Net Sales. The Company's 2020 second quarter sales of $21,818,000 decreased $4,991,000 or 18.6% compared to the second quarter of 2019, which generated sales of $26,809,000. The decrease in sales resulted mostly from a decrease in unit volume, slightly offset by pricing actions which the Company took to offset material cost pressure and to protect margins.

Gross Profit. The Company's gross profit margins were 60.8% and 62.4% for the three months ended June 30, 2020 and 2019, respectively. The Company experienced a decrease in production during the first six months of 2020, which diminished labor and overhead absorption, and resulted in lower gross profit.

Selling Expenses. Selling expenses consist primarily of employee salaries and associated overhead costs, commissions, and the cost of marketing programs such as advertising, trade shows and related communication costs, and freight. Selling expense was $3,503,000 and $4,300,000 for the three months ended June 30, 2020 and 2019, respectively, representing a decrease of $797,000 or 18.5%. The decrease was mostly related to lower commissions and freight expenses, which move in relation to sales. Selling expenses as a percent of net sales were identical to last year, being 16.0% for the three months ended June 30, 2020 and 2019.

General and Administrative Expenses. General and administrative expenses consist primarily of employee salaries, benefits for administrative, executive and finance personnel, legal and accounting, and corporate general and administrative services. General and administrative expenses were $3,852,000 and $6,140,000 for the three-months ended June 30, 2020 and 2019, respectively, thus decreasing by $2,298,000 or 37.3%. The Company experienced a reduction in legal and product liability related defense costs of $2,329,000 in 2020 mostly related to a slow-down in the ongoing class action case which is being vigorously defended. The decrease in legal costs was slightly offset by an increase in the phantom stock component of incentive compensation, associated with the increase in the Company's stock price during the recent quarter. As a percentage of sales, general and administrative expenses decreased to 17.7% for the three months ended June 30, 2020 from 22.9% for the three months ended June 30, 2019.

Engineering Expense. Engineering expenses consist of development expenses associated with the development of new products and enhancements to existing products, and manufacturing engineering costs. Engineering expenses were $1,021,000 and $1,152,000 for the three months ended June 30, 2020 and 2019, respectively, decreasing by $131,000 or 11.4%, partially associated with a reduction in experimental materials previously required for the progression of various promising applications. Engineering expenses increased modestly as a percentage of sales, being 4.7% for the three months ended June 30, 2020, and 4.3% for the same period in 2019.

Operating Profits. Reflecting all of the factors mentioned above, operating profits were $4,886,000 and $5,144,000 for the quarters ending June 30, 2020 and 2019, respectively, decreasing by $258,000 or 5.0%. As a percentage of sales, operating profits increased, being 22.4% and 19.2% for the three-months ended June 30, 2020 and 2019, respectively.

Interest Income (Expense)-Net. Interest income is recorded on cash investments, and interest expense is recorded at times when the Company has debt amounts outstanding on its line of credit. The Company recorded $97,000 of interest expense and $236,000 of interest income during the second quarters of 2020 and 2019, respectively. The reduction in interest income was largely due to the lower cash balance and thus lack of investment, mostly resulting from the $35,330,000 special dividend paid in December 2019. Additionally, the Company had borrowed

$15,000,000 on its line of credit for a portion of the second quarter of 2020 to ensure liquidity during the COVID-19 crisis.

Other Income (Expense)-Net. Other Income (Expense)-net primarily consists of foreign currency exchange gains (losses) on transactions settled in currencies other than the Company's local currency, typically related to the Company's foreign UK subsidiaries. There was expense of $23,000 and $33,000 recorded during the second quarters of 2020 and 2019, respectively.

Income Tax Expense. Income Tax Expense was $1,196,000 for the second quarter of 2020, compared to $1,325,000 for the same period in 2019, decreasing $129,000 or 9.7%, mostly the result of the decrease in income before taxes.

**Six months ended June 30, 2020 vs. June 30, 2019**

The Company reported comparative results from continuing operations for the six months ended June 30, 2020 and 2019 as follows:

| | **Six months ended June 30,** (in thousands) | | | |
|---|---|---|---|---|
| | **2020** | **2020** | **2019** | **2019** |
| | **($000)** | **%** | **($000)** | **%** |
| Net Sales | $47,084 | 100.0% | $53,597 | 100.0% |
| Gross Profit | $29,031 | 61.7% | $33,682 | 62.8% |
| Operating Profit | $10,731 | 22.8% | $10,735 | 20.0% |

Net Sales. The Company's sales for the first six months of 2020 of $47,084,000 decreased $6,513,000 or 12.2% over the first six months of 2019, which generated sales of $53,597,000. The decrease in sales resulted mostly from a decrease in unit volume, slightly offset by pricing actions which the Company took to offset material cost pressure and to protect margins.

Gross Profit. The Company's gross profit margins were 61.7% and 62.8% for the six months ended June 30, 2020 and 2019, respectively. The Company experienced a decrease in production during the first six months of 2020, most notably during the second quarter as a result of COVID-19, which diminished labor and overhead absorption, and resulted in lower gross profit.

Selling Expenses. Selling expenses consist primarily of employee salaries and associated overhead costs, commissions, and the cost of marketing programs such as advertising, trade shows and related communication costs, and freight. Selling expense was $8,054,000 and $8,810,000 for the six months ended June 30, 2020 and 2019, respectively, representing a decrease of $756,000 or 8.6%. The decrease was mostly related to lower commissions and freight expenses, which move in relation to sales. Travel and advertising costs were also lower. Selling expenses as a percent of net sales compared to last year, were 17.1% for the six months ended June 30, 2020, and 16.4% for the six months ended June 30, 2019, increasing slightly.

General and Administrative Expenses. General and administrative expenses consist primarily of employee salaries, benefits for administrative, executive and finance personnel, legal and accounting, and corporate general and administrative services. General and administrative expenses were $8,105,000 and $11,644,000 for the six months ended June 30, 2020 and 2019, respectively, thus decreasing by $3,539,000 or 30.4%. The Company experienced a reduction in legal and product liability related defense costs of $2,681,000 in 2020 mostly related to a slow-down in the ongoing class action case which is being vigorously defended. The Company also experienced a decrease in the phantom stock portion of incentive compensation expense between years associated with the contrast in movement of the Company's stock over the respective six-month period. A decrease in director compensation also occurred, as there was a distribution of shares awarded to the non-employee directors in June 2019, but no such grant during 2020. As a percentage of sales, general and administrative expenses decreased to 17.2% for the six months ended June 30, 2020 from 21.7% for the six months ended June 30, 2019.

Engineering Expense. Engineering expenses consist of development expenses associated with the development of new products and enhancements to existing products, and manufacturing engineering costs. Engineering expenses were $2,141,000 and $2,493,000 for the six months ended June 30, 2020 and 2019, respectively, decreasing by $352,000 or 14.1%. The decrease was primarily attributable to a reduction in experimental materials that diminished after the completion of work on various promising applications during 2019. Engineering expenses decreased as a percentage of sales, being 4.6% for the six months ended June 30, 2020, and 4.7% for the same period in 2019.

Operating Profits. Reflecting all of the factors mentioned above, operating profits were $10,731,000 and $10,735,000 for the six months ended June 30, 2020 and 2019, respectively, decreasing by $4,000, essentially flat. As a percentage of sales, operating profits increased, being 22.8% and 20.0% for the six-months ended June 30, 2020 and 2019, respectively.

Interest Income (Expense)-Net. Interest income is recorded on cash investments, and interest expense is recorded at times when the Company has debt amounts outstanding on its line of credit. The reduction in interest income was largely due to the lower cash balance and thus lack of investment, mostly resulting from the $35,330,000 special dividend paid in December 2019. Additionally, the Company had borrowed $15,000,000 on its line of credit for a portion of the second quarter of 2020 to ensure liquidity during the COVID-19 crisis.

Other Income (Expense)-Net. Other Income (Expense)-net primarily consists of foreign currency exchange gains (losses) on transactions with Omega Flex Limited, our UK subsidiary. There was expense of $131,000 recorded during the first six months of 2020, and income of $5,000 for the same period in 2019.

Income Tax Expense. Income Tax Expense was $2,612,000 for the first six months of 2020, compared to $2,743,000 for the same period in 2019. The $131,000 or 4.8% decrease in the tax expense was largely the result of the decrease in income before taxes.

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

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

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

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

### **Revenue Recognition**

According to Accounting Standards Update 2014-09, *Revenue from Contracts with Customers (Topic 606)*, the Company recognizes revenue in a manner to depict the transfer of goods or services to a customer at an amount that reflects the consideration expected to be received in exchange for those goods or services.

The principle of Topic 606 is achieved through applying the following five-step approach:

- *Identification of the contract, or contracts, with a customer* — a contract with a customer exists when the Company enters into an enforceable contract with a customer, typically a purchase order initiated by the customer, that defines each party's rights regarding the goods to be transferred and identifies the payment terms related to these goods.

- *Identification of the performance obligations in the contract* — performance obligations promised in a contract are identified based on the goods that will be transferred to the customer that are distinct, whereby the customer can benefit from the goods on their own or together with other resources that are readily available from third parties or from us. Persuasive evidence of an arrangement for the sale of product must exist. The Company ships product in accordance with the purchase order and standard terms as reflected within the Company's order acknowledgments and sales invoices.

- *Determination of the transaction price* —the transaction price is determined based on the consideration to which the Company will be entitled in exchange for transferring goods to the customer. This would be the agreed upon quantity and price per product type in accordance with the customer purchase order, which is aligned with the Company's internally approved pricing guidelines.

- *Allocation of the transaction price to the performance obligations in the contract* — if the contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. This applies to the Company as there is only one performance obligation to ship the goods.

- *Recognition of revenue when, or as, the Company satisfies a performance obligation* — the Company satisfies performance obligations at a point in time when control of the goods transfers to the customer. Determining the point in time when control transfers requires judgment. Indicators considered in determining whether the customer has obtained control of a good include:

  - The Company has a present right to payment
  - The customer has legal title to the goods
  - The Company has transferred physical possession of the goods
  - The customer has the significant risks and rewards of ownership of the goods
  - The customer has accepted the goods

  It is important to note that the indicators are not a set of conditions that must be met before the Company can conclude that control of the goods has transferred to the customer. The indicators are a list of factors that are often present if a customer has control of the goods.

  The Company has typical, unmodified FOB shipping point terms. As the seller, the Company can determine that the shipped goods meet the agreed-upon specifications in the contract or customer purchase order (e.g. items, quantities, and prices) with the buyer, so customer acceptance would be deemed a formality, as noted in ASC 606-10-55-86. As a result, the Company has a legal right to payment upon shipment of the goods.

  Based upon the above, the Company has concluded that transfer of control substantively transfers to the customer upon shipment.

Other considerations of Topic 606 include the following:

- *Contract Costs* - costs to obtain a contract (e.g. customer purchase order) include sales commissions. Under Topic 606, these costs may be expensed as incurred for contracts with a duration of one year or less. The majority of the Company's customer purchase orders are fulfilled (e.g. goods are shipped) within two days of receipt.

- *Warranties* - the Company does not offer customers to purchase a warranty separately. Therefore, there is not a separate performance obligation. The Company does account for warranties as a cost accrual and the warranties do not include any additional distinct services other than the assurance that the goods comply with agreed-upon specifications. There is no impact of warranties under Topic 606 upon the financial reporting of the Company.

- *Returned Goods* - from time to time, the Company provides authorization to customers to return goods. If deemed to be material, the Company would record a "right of return" asset for the cost of the returned goods which would reduce cost of sales.

- *Volume Rebates (Promotional Incentives)* - volume rebates are variable (dependent upon the volume of goods purchased by our eligible customers) and, under Topic 606, must be estimated and recognized as a reduction of revenue as performance obligations are satisfied (e.g. upon shipment of goods). Also under Topic 606, to ensure that revenue recognized would not be probable of a significant reversal, the four following factors are considered:

  - The amount of consideration is highly susceptible to factors outside the Company's influence.
  - The uncertainty about the amount of consideration is not expected to be resolved for a long period of time.
  - The Company's experience with similar types of contracts is limited.
  - The contract has a large number and broad range of possible consideration amounts.

  If it was concluded that the above factors were in place for the Company, it would support the probability of a significant reversal of revenue. However, as none of the four factors apply to the Company, promotional incentives are recorded as a reduction of revenue based upon estimates of the eligible products expected to be sold.

Regarding disaggregated revenue disclosures, as previously noted, the Company's business is controlled as a single operating segment that consists of the manufacture and sale of flexible metal hose. Most of the Company's transactions are very similar in nature, contract, terms, timing, and transfer of control of goods. As indicated within Note 2, under the caption "Significant Concentration", the majority of the Company's sales were geographically contained within North America, with the remainder scattered internationally. All performance assessments and resource allocations are generally based upon the review of the results of the Company as a whole.

**<u>Cash Equivalents</u>**

The Company considers all highly liquid investments with an original maturity of 90 days or less at the time of purchase to be cash equivalents. Cash equivalents include investments in an institutional money market fund, which invests in U.S. Treasury bills, notes and bonds, and/or repurchase agreements, backed by such obligations. Carrying value approximates fair value. Cash and cash equivalents are deposited at various area banks, which at times may exceed federally insured limits. The Company monitors the viability of the banking institutions carrying its assets on a regular basis, and has the ability to transfer cash to various institutions during times of risk. The Company has not experienced any losses related to these cash balances, and believes its credit risk to be minimal.

**Accounts Receivable and Provision for Credit Losses**

All accounts receivables are stated at amortized cost, net of allowances for credit losses, and adjusted for any write-offs. The Company maintains allowances for credit losses, which represent an estimate of expected losses over the remaining contractual life of its receivables considering current market conditions and estimates for supportable forecasts when appropriate. The estimate is a result of the Company's ongoing assessments and evaluations of collectability, historical loss experience, and future expectations in estimating credit losses in its receivable portfolio. For accounts receivables, the Company uses historical loss experience rates and applies them to a related aging analysis while also considering customer and/or economic risk where appropriate. Determination of the proper amount of allowances requires management to exercise judgment about the timing, frequency and severity of credit losses that could materially affect the provision for credit losses and, as a result, net earnings. The allowances consider numerous quantitative and qualitative factors that include receivable type, historical loss experience, delinquency trends, collection experience, current economic conditions, estimates for supportable forecasts, when appropriate, and credit risk characteristics.

The reserve for credit losses, which include future credits, discounts, and doubtful accounts, was $887,000 and $1,433,000 as of June 30, 2020 and December 31, 2019, respectively.

**Investments**

The Company invests excess funds in liquid interest earning instruments including U.S. Treasury bills and bank time deposits, with maturities typically of one year or less. These investments are stated at fair value, which approximates amortized cost, and are classified as available-for-sale in accordance with ASC 320, *Investments – Debt and Equity Securities*. The Company did not have any investments as of June 30, 2020 and December 31, 2019, respectively.

**Inventories**

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

**Property and Equipment**

Property and equipment are initially recorded at cost. Depreciation and amortization are computed using the straight-line method over the estimated useful lives of the assets or, for leasehold improvements, the life of the lease, if shorter. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is reflected in other income or expense for the period. The cost of maintenance and repairs is expensed as incurred; significant improvements are capitalized.

**Goodwill**

In accordance with Financial Accounting Standards Board ("FASB") ASC Topic 350, *Intangibles – Goodwill and Other*, the Company performed an annual impairment test as of December 31, 2019. This analysis did not indicate any impairment of goodwill.

However, the duration and severity of the COVID-19 pandemic could result in future goodwill impairment charges. While we have concluded that a triggering event did not occur during the six months ended June 30, 2020, a prolonged pandemic could impact the Company's results of operations in a manner significant enough to trigger an interim impairment test.

**Stock-Based Compensation Plans**

In 2006, the Company adopted a Phantom Stock Plan (the "Plan"), which allows the Company to grant phantom stock units ("Units") to certain key employees, officers or directors. The Units each represent a contractual right to payment of compensation in the future based upon the market value of the Company's common stock. The Units follow a vesting schedule of three years from the grant date, and are then paid upon maturity. In accordance with FASB ASC Topic 718, *Compensation* - *Stock Compensation*, the Company uses the Black-Scholes option pricing model as its method for determining the fair value of the Units and are accordingly recorded as liabilities. Additionally, the liabilities for the Units are adjusted to market value over time from the grant dates to the related maturity dates. Further details of the Plan are provided in Note 6.

**Product Liability Reserves**

Product liability reserves represent the estimated unpaid amounts under the Company's insurance policies with respect to existing claims. The Company uses the most current available data to estimate claims. As explained more fully under Note 5, Commitments and Contingencies, for various product liability claims covered under the Company's general liability insurance policies, the Company must pay certain defense and settlement costs within its deductible or self-insured retention limits, ranging primarily from $25,000 to $1,000,000 per claim, depending on the terms of the policy in the applicable policy year, up to an aggregate amount. The Company is vigorously defending against all known claims.

**Leases**

Effective January 1, 2019, the Company adopted the requirements of FASB ASU 2016-02, *Leases* (Topic 842) which defines a lease as any contract that conveys the right to use a specific asset for a period of time in exchange for consideration. Leases are classified as a finance lease, formerly called a capital lease, if any of the following criteria are met:

1. The lease transfers ownership of the underlying asset to the lessee by the end of the lease term.
2. The lease grants the lessee an option to purchase the underlying asset that the lessee is reasonably certain to exercise.

3. The lease term is for the major part of the remaining economic life of the underlying asset.
4. The present value of the sum of lease payments and any residual value guaranteed by the lessee equals or exceeds substantially all of the fair value of the underlying asset.
5. The underlying asset is of such a specialized nature that it is expected to have no alternative use to the lessor at the end of the lease term.

For any leases that do not meet the criteria identified above for finance leases, the Company treats such leases as operating leases. As of June 30, 2020, each of the Company's leases are classified as operating leases.

Both finance and operating leases are reflected on the balance sheet as lease or "right-of-use" assets and lease liabilities.

There are some exceptions, which the Company has elected in its accounting policies. For leases with terms of twelve months or less, or below the Company's general capitalization policy threshold, the Company has elected an accounting policy to not recognize lease assets and lease liabilities for all asset classes. The Company recognizes lease expense for such leases generally on a straight-line basis over the lease term.

The Company determines if a contract is a lease at the inception of the arrangement. The Company reviews all options to extend, terminate, or purchase its right-of-use assets at the inception of the lease and accounts for these options when they are reasonably certain to be exercised. Certain leases contain non-lease components, such as common area maintenance, which are generally accounted for separately. In general, the Company will assess if non-lease components are fixed and determinable, or variable, when determining if the component should be included in the lease liability. For purposes of calculating the present value of the lease obligations, the Company utilizes the implicit interest rate within the lease agreement when known and/or determinable, and otherwise utilizes its incremental borrowing rate at the time of the lease agreement.

As permitted under ASU 2018-11, the Company elected the optional transition method to adopt the new leases standard. Under this new transition method, the Company initially applied the new leases standard at the adoption date of January 1, 2019 and would have recognized a cumulative-effect adjustment, if appropriate, to the opening balance of retained earnings in the period of adoption. No cumulative-effect adjustment was recognized.

The impact of the adoption of this new standard resulted in an increase to the Company's operating lease assets and liabilities on January 1, 2019 of approximately $800,000. The implementation did not have a material impact on our consolidated statements of income and statements of cash flows.

**<u>Fair Value of Financial and Nonfinancial Instruments</u>**

The Company measures financial instruments in accordance with FASB ASC Topic 820, *Fair Value Measurements and Disclosures*. The accounting standard defines fair value, establishes a framework for measuring fair value under GAAP, and enhances disclosures about fair value measurements. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard creates a fair value hierarchy which prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as follows: Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities; Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and Level 3 inputs are unobservable inputs that reflect the Company’s own assumptions about the assumptions market participants would use in pricing the asset or liability. The Company relies upon Level 1 inputs in determining the fair value of investments and the fair value of the Company’s reporting unit in its annual impairment test as described in the FASB ASC Topic 350, *Intangibles - Goodwill and Other*.

**Earnings per Common Share**

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

**Currency Translation**

Assets and liabilities denominated in foreign currencies, most of which relate to the Company’s United Kingdom subsidiary whose functional currency is British pound sterling, are translated into U.S. dollars at exchange rates prevailing on the balance sheet dates. The statements of income are translated into U.S. dollars at average exchange rates for the period. Adjustments resulting from the translation of financial statements are excluded from the determination of income and are accumulated in a separate component of shareholders’ equity. Exchange gains and losses resulting from foreign currency transactions are included in the statements of income (other expense) in the period in which they occur.

**Income Taxes**

The Company accounts for tax liabilities in accordance with the FASB ASC Topic 740, Income Taxes. Under this method the Company recorded tax expense, related deferred taxes and tax benefits, and uncertainties in tax positions.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities from a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is provided for deferred tax assets if it is more likely than not that these items will either expire before the Company is able to realize the benefit, or that future deductibility is uncertain.

The FASB ASC Topic 740, Income Taxes, clarifies the criteria that an individual tax position must satisfy for some or all of the benefits of that position to be recognized in a company's financial statements. This guidance prescribes a recognition threshold of more-likely than-not, and a measurement attribute for all tax positions taken or expected to be taken on a tax return, in order for those tax positions to be recognized in the financial statements.

The Company follows the provisions of ASC 740-10 relative to accounting for uncertainties in tax positions. These provisions provide guidance on the recognition, de-recognition and measurement of potential tax benefits associated with tax positions.

On March 27, 2020, the Coronavirus Aid, Relief, and Economic Security (CARES) Act was signed into law making several changes to the Internal Revenue Code. The changes include, but are not limited to: increasing the limitation on the amount of deductible interest expense, allowing companies to carryback certain net operating losses, and increasing the amount of net operating loss carryforwards that corporations can use to offset taxable income. The tax law changes in the Act have not had an effect on the Company's income tax provision for the three and six months ended June 30, 2020.

**Other Comprehensive Income**

For the three and six months ended June 30, 2020 and 2019, respectively, the components of other comprehensive income consisted solely of foreign currency translation adjustments.

**Significant Concentration**

The Company has one significant customer which represented more than 10% of the Company's Accounts Receivable at June 30, 2020 and December 31, 2019. That same customer represented more than 10% of the Company's total Net Sales for the three and six months ended June 30, 2020 and 2019, respectively. Geographically, the Company has a significant amount of sales in the United States versus internationally. These concentrations are consistent with those discussed in detail in the Company's December 31, 2019 Form 10-K.

**Subsequent Events**

The Company evaluates all events or transactions through the date of the related filing that may have a material impact on its condensed consolidated financial statements. Refer to Note 10 of the condensed consolidated financial statements.

**Recent Accounting Pronouncements**

In January 2017, the FASB amended ASC Topic 350, *Intangibles – Goodwill and Other* (issued under ASU 2017-04, "Simplifying the Test for Goodwill Impairment"). This amendment simplifies the test for goodwill impairment by only requiring an entity to perform an annual or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and recognizes an impairment charge for the amount that the carrying amount exceeds the reporting unit's fair value. Any loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. The amendment required adoption on January 1, 2020. In compliance, the Company adopted ASU 2017-04 as required during the first quarter of 2020 and determined that there was no material impact on its condensed consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 replaced the incurred loss impairment methodology under current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. ASU 2016-13 requires use of a forward-looking expected credit loss model for accounts receivables, loans, and other financial instruments. ASU 2016-13 is effective for fiscal years beginning after December 15, 2019, with early adoption permitted. Adoption of the standard requires using a modified retrospective approach through a cumulative-effect adjustment to retained earnings as of the effective date to align existing credit loss methodology with the new standard. In November 2019, the FASB issued ASU 2019-11, Codification Improvements to Topic 326, Financial Instruments—Credit Losses. ASU 2019-11 requires entities that did not adopt the amendments in ASU 2016-13 as of November 2019 to adopt ASU 2019-11. This ASU contains the same effective dates and transition requirements as ASU 2016-13. We adopted ASU 2016-13 and ASU 2019-11 effective January 1, 2020. The impact of adoption of these standards on our condensed consolidated financial statements was not material.

## LIQUIDITY AND CAPITAL RESOURCES

Historically, the Company's primary cash needs have been related to working capital items, which the Company has largely funded through cash generated from operations.

As of June 30, 2020, the Company had a cash balance of $19,487,000. Additionally, the Company has a $15,000,000 line of credit available, as discussed in detail in Note 4, which had no borrowings outstanding upon it at June 30, 2020. At December 31, 2019, the Company had a cash balance of $16,098,000, with no borrowings against the line of credit.

We believe our existing cash and cash equivalents, along with our borrowing capacity, will be sufficient to meet our anticipated cash needs for at least the next twelve months. Our future capital requirements will depend upon many factors including our rate of revenue growth, the timing and extent of any expansion efforts, the potential for investments in, or the acquisition of any complementary products, businesses or supplementary facilities for additional capacity, and the COVID-19 pandemic. The details of our operating, investing and financing activities are provided below.

### Operating Activities

Cash provided by operating activities is net income adjusted for certain non-cash items and changes in certain assets and liabilities, such as those included in working capital.

For the first six months of 2020, the Company's operating activities provided cash of $9,303,000, compared to the first six months of 2019 which provided cash of $5,079,000, a difference of $4,224,000. For details of the operating cash flows refer to the condensed consolidated statements of cash flows in Part I – Financial Information on page seven.

**Investing Activities**

Cash used in investing activities during the first six months of 2020 and 2019 was $187,000 and $8,676,000, respectively. For these same periods, cash used for capital expenditures was $187,000 and $722,000, respectively, decreasing by $535,000. For 2019, cash was used to purchase short-term investments of $22,954,000, which was partially offset by cash received from net proceeds from the sale of short-term investments of $15,000,000.

**Financing Activities**

All financing activities relate to dividend payments, which are detailed in Note 8, Shareholders' Equity. Dividend payments through the first six months of 2020 and 2019, amounted to $5,653,000 and $4,844,000 respectively. See Note 4, Line of Credit and Other Borrowings, for a description of borrowings and repayments during the second quarter of 2020.

## CONTINGENT LIABILITIES AND GUARANTEES

See Note 5 to the Company's condensed consolidated financial statements.

## OFF-BALANCE SHEET ARRANGEMENTS

None

## Item 3 – Quantitative and Qualitative Information about Market Risks

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

## Item 4 – Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures.

At the end of the fiscal second quarter of 2020, the Company evaluated the effectiveness of the design and operation of its disclosure controls and procedures. The Company's disclosure controls and procedures are designed to ensure that the Company records, processes, summarizes and reports in a timely manner the information required to be disclosed in the periodic reports filed by the Company with the Securities and Exchange Commission. The Company's management, including the chief executive officer and chief financial officer, have conducted an evaluation of the effectiveness of the design and operation of the Company's Disclosure Controls and Procedures as defined in the Rule 13a-15(e) of Securities Exchange Act of 1934. Based on that evaluation, the chief executive officer and chief financial officer have concluded that, as of the date of this report, the Company's disclosure controls and procedures are effective to provide reasonable assurance of achieving the purposes described in Rule 13a-15(e), and no changes are required at this time.

(b) Changes in Internal Controls.

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

## PART II - OTHER INFORMATION

### Item 1 – Legal Proceedings

In the ordinary and normal conduct of the Company's business, it is subject to periodic lawsuits, investigations and claims (collectively, the "Claims"). Most of the Claims, including a putative class-action claim, relate to potential lightning damage to our flexible gas piping products, which impact legal and product liability related expenses. The Company does not believe the Claims have legal merit, and therefore has commenced a vigorous defense in response to the Claims. It is possible that the Company may incur increased litigation costs in the future due to a variety of factors, including a higher number of Claims, higher legal costs, and higher insurance deductibles or retentions.

In June 2017, a putative class action case was re-filed against the Company and other parties in Missouri state court after the predecessor case was dismissed without prejudice by the federal court. The Company successfully removed the case to federal court and is currently vigorously defending the case.

The Company was made aware of a potential legal liability regarding a legal dispute in the United Kingdom, in which the Company's subsidiary, Omega Flex Limited ("OFL"), was the claimant. After reviewing currently available information, there are a range of possible outcomes; (1) from British Standards Institution ("BSI"), the defendant, paying OFL a portion of its legal costs incurred in the action, (2) to each side bearing its own costs, or (3) OFL paying a portion of BSI's legal costs. The potential amount of loss in the last outcome (paying BSI's legal costs) is estimated to be between $200,000 and $500,000. No amounts have been recorded for the potential liability at this time due to the uncertainty of the ultimate outcome, and the potential loss is not deemed probable.

The Company has in place commercial general liability insurance policies that cover most Claims, which are subject to deductibles or retentions, ranging primarily from $25,000 to

$1,000,000 per claim (depending on the terms of the policy and the applicable policy year), up to an aggregate amount. Litigation is subject to many uncertainties and management is unable to predict the outcome of the pending suits and claims. The potential liability for a given claim could range from zero to a maximum of $1,000,000, depending upon the circumstances, and insurance deductible or retention in place for the respective claim year. The aggregate maximum exposure for all current open Claims, excluding the Missouri class action case, as of June 30, 2020 is estimated to not exceed approximately $5,800,000, which represents the potential costs that may be incurred over time for the Claims within the applicable insurance policy deductibles or retentions. From time to time, depending upon the nature of a particular case, the Company may decide to spend in excess of a deductible or retention to enable more discretion regarding the defense, although this is not common. It is possible that the results of operations or liquidity of the Company, as well as the Company's ability to procure reasonably priced insurance, could be adversely affected by the pending litigation, potentially materially. The Company is currently unable to estimate the ultimate liability, if any, that may result from the pending litigation, or potential litigation from future claims or claims that have not yet come to our attention, and accordingly, the liability in the consolidated financial statements primarily represents an accrual for legal costs for services previously rendered, and outstanding or anticipated settlements for Claims. The liabilities recorded on the Company's books at June 30, 2020 and December 31, 2019 were $150,000 and $215,000, respectively, and are included in Other Liabilities.

## Item 1A – Risk Factors

In addition to the risk factors described under Item 1A of the Company's Form 10-K for the year ended December 31, 2019, readers should also carefully consider the risks, uncertainties and other factors described below, in addition to the other information set forth in this report, because they could materially and adversely affect the Company's business, operating results, financial condition, cash flows, prospects, and the value of an investment in the Company's common stock.

*Risks Related to Our Business*

**The COVID-19 pandemic has begun to affect and may continue to affect the business.**

The ongoing global outbreak of coronavirus, which was declared a pandemic by the World Health Organization on March 11, 2020 and a national emergency by the President of the United States on March 13, 2020, has caused and is continuing to cause business slowdowns and shutdowns and turmoil in the financial markets both in the United States and abroad. The Company is monitoring the impact of the COVID-19 pandemic on its business, including how it has impacted and will impact the Company's employees, customers, suppliers and distribution channels. The COVID-19 pandemic, as well as the quarantines and other governmental and non-governmental restrictions that have been imposed throughout the world in an effort to contain or mitigate the spread of the coronavirus, has created significant volatility, uncertainty and economic disruption which has begun to affect and may continue to affect the Company's business. For example, governmental authorities in several jurisdictions have ordered the cessation of all business activity that is deemed non-essential and, although the Company's business has to date been deemed essential in many affected markets, there is a risk that these shutdown orders will be extended or expanded or that similar shutdown orders will be implemented in other regions.

While the Company has not yet seen a material impact from the COVID-19 pandemic on its business, financial position, liquidity, or ability to service customers or maintain critical operations, the Company is currently navigating through this unprecedented crisis without any government support from the U.S. Small Business Administration's Paycheck Protection Program ("PPP"), and the nature and magnitude of the COVID-19 pandemic's ultimate impact on the Company will depend on numerous evolving factors, future developments and cascading effects of the coronavirus pandemic that the Company is not able to predict, including: the duration and severity of the COVID-19 pandemic and the international actions and business restrictions that are being undertaken and implemented as a result of it; governmental, business and other responses to the COVID-19 pandemic, including the promotion of "social distancing," the issuance of shelter in place orders and restrictions on the Company's operations, and the possibility that government officials may mandate that the Company provide products or services; potential disruptions in the Company's supply chain; the impact of the COVID-19 pandemic on the Company's ability to execute its short-term and long-term business strategies and initiatives; the extent to which forced remote working arrangements reduce the Company's ability to manage its business effectively; the extent to which staffing shortages due to members of the Company's workforce being quarantined or exposed to the coronavirus may be detrimental to the Company's operations; and the Company's ability to maintain current levels of skilled headcount without the proceeds of the loan under the PPP (the "PPP Loan") as a source of additional liquidity. Furthermore, while the Company timely returned the proceeds of its PPP Loan out of an abundance of caution in reliance on U.S. Treasury Department and Small Business Administration guidance that companies were able to do so without penalty, as the COVID-19 pandemic unfolds, federal or state governments (including government agencies such as the Treasury Department, the Small Business Administration or the SEC) could promulgate new statutes, regulations, guidance or relief measures, or rescind or modify existing statutes, regulations, guidance or relief measures, in a way that is detrimental to the Company or its business, including as a result of the Company's prior application for a loan under the PPP.

In addition, while the Company cannot predict the magnitude of the impact that the COVID-19 pandemic will have on its customers and suppliers or their financial conditions, any material effect on the Company's customers or suppliers could adversely impact the Company. For example, the Company's customers or suppliers may themselves assert, or attempt to terminate various agreements and arrangements with us on the basis of, contractual force majeure provisions, and any termination of a significant commercial agreement may adversely harm our operations. Additionally, the COVID-19 pandemic and related travel restrictions and other containment efforts have had a significant impact on the travel industry, which may result in reduced demand for products. The impact of the COVID-19 pandemic may also exacerbate other risk factors described under Item 1A of the Company's Form 10-K for the year ended December 31, 2019, any of which could have a material effect on the Company. For example, the risks associated with potential cybersecurity threats may be magnified given the increase in the number of Company employees working remotely using personal electronic devices and home internet connections.

The extent of the impact of the COVID-19 pandemic on the Company's business is highly uncertain and difficult to predict, as information is rapidly evolving with respect to the duration and severity of the COVID-19 pandemic. At this point, the Company cannot reasonably estimate the duration and severity of the COVID-19 pandemic or its overall impact on the Company's business.

**Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds**

None.

**Item 3 – Defaults Upon Senior Securities**

None.

**Item 4 – Mine Safety Disclosures**

Not Applicable.

**Item 5 – Other Information**

None.

**Item 6 - Exhibits**

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

## SIGNATURES

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

OMEGA FLEX, INC.
(Registrant)

Date: August 3, 2020

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

**EXHIBIT 31.1**

Certification by the Chief Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Kevin R. Hoben, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for fiscal quarter ended June 30, 2020, of Omega Flex, Inc. (the "registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 3, 2020

/s/ Kevin R. Hoben

Kevin R. Hoben
Chief Executive Officer

**EXHIBIT 31.2**

Certification by the Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Paul J. Kane, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for fiscal quarter ended June 30, 2020, of Omega Flex, Inc. (the “registrant”);

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 3, 2020

/s/ Paul J. Kane

Paul J. Kane
Chief Financial Officer

**EXHIBIT 32.1**

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO SECTION 906 OF
THE SARBANES-OXLEY ACT OF 2002

Each of the undersigned hereby certifies, for the purposes of 18 U.S.C. Section 1350, in his capacity as an officer of Omega Flex, Inc. (the “Company”), that, to his knowledge:

(a) the Quarterly Report on Form 10-Q of the Company for the fiscal quarter ended June 30, 2020, as filed with the Securities and Exchange Commission (the “Report”), fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934; and

(b) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 3, 2020

/s/ Kevin R. Hoben

Kevin R. Hoben
Chief Executive Officer

/s/ Paul J. Kane

Paul J. Kane
Chief Financial Officer

This certification is not deemed to be “filed” for purposes of section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section. This certification is not deemed to be incorporated by reference into any filing under the Securities Act of 1933 or Securities Exchange Act of 1934, except to the extent that the Company specifically incorporates it by reference.