FLANDERS CORP
Form 10-K
February 24, 2004

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

[X]

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the year ended December 31, 2003

or

[ ]

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from ____________________ to _____________________

Commission File Number 0-27958

FLANDERS CORPORATION

(Exact name of registrant as specified in its charter)

North Carolina	13-3368271
(State or other jurisdiction of incorporation or organization)	(IRS Employer ID Number)
2399 26th Avenue North, St. Petersburg, FL	33734
(Address of principal executive offices)	(Zip Code)

Registrants telephone number, including area code: (727) 822-4411

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

Title of each class

Common Stock, $.001 per share par value

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrants knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

YES___

NO _X_

As of March 26, 2003, the aggregate market value of the voting stock held by non-affiliates of the registrant was approximately

$26.3 million.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

YES___

NO _X_

As of February 23, 2004, the number of shares outstanding of the registrants common stock was 26,151,846 shares.

Documents incorporated into this report on Form 10-K by reference: None.

FLANDERS CORPORATION

FORM 10-K

FOR THE YEAR ENDED DECEMBER 31, 2003

TABLE OF CONTENTS

SIGNATURES

FINANCIAL STATEMENTS

*The report of Grant Thornton, which is limited to the statements of operations, stockholders equity and cash flows for the year ended 2001, which was previously provided by Grant Thornton in prior filings, is not included herein.

PART I

Item 1.

Business

OVERVIEW

We design, manufacture and market air filters and related products, and are focused on providing complete environmental filtration systems for end uses ranging from controlling contaminants in residences and commercial office buildings through specialized manufacturing environments for semiconductors and pharmaceuticals. Currently, we believe, based on available trade and industry data, that we are one of the largest domestic manufacturers of air filters that are utilized by many industries including those associated with commercial and residential heating, ventilation and air conditioning systems (commonly known as HVAC systems), semiconductor manufacturing, ultra-pure materials, nuclear power and materials processing, biotechnology, pharmaceuticals, synthetics, nuclear power and nuclear materials processing. We also design and manufacture much of our own production equipment to automate our processes in order to decrease labor costs associated with our standard products. Additionally, we produce glass-based air filter media for many of our products. Our customers include Abbott Laboratories, The Home Depot, Inc., Motorola, Inc., Merck & Co., Inc., Upjohn Co., Wal-Mart Stores, Inc., Westinghouse Electric Corp., and several large computer chip manufacturers.

The majority of our revenues come from the sale of after-market replacement filters, since air filters are typically placed in equipment designed to last much longer than the filters.

GENERAL DEVELOPMENT OF BUSINESS

Flanders Corporation was originally incorporated on July 2, 1986 in the State of Nevada, but is currently incorporated in the State of North Carolina. Our principal executive offices are currently located at 2399 26th Avenue North, St. Petersburg, FL 33734. The Company s internet website address is www.flanderscorp.com. The information contained on our website is not part of our reports with the Securities and Exchange Commission and is not incorporated by reference into this report. The Company s annual reports on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K, and all amendments thereto, are available free of charge on the Company s website as soon as reasonably practicable after such reports are electronically filed with, or furnished to, the Securities and Exchange Commission.

FORWARD-LOOKING STATEMENTS AND ASSOCIATED RISKS

This annual report, including all documents incorporated herein by reference, includes certain forward-looking statements within the meaning of that term in Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934, including, among others, those statements preceded by, following or including the words believe, expect, anticipate or similar expressions. These forward-looking statements are based largely on the current expectations of management and are subject to a number of risks and uncertainties. Actual results could differ materially from these forward-looking statements. In addition to the other risks described in the Factors That May Affect Future Results discussion under Management s Discussion and Analysis of Financial Condition and Results of Operations in Part II of this annual report, important factors to consider in evaluating such forward-looking statements include risks associated with demand for our products, market acceptance, economic conditions, competitive products and pricing, difficulties in product development, commercialization and technology. In light of these risks and uncertainties, there can be no assurance that the events contemplated by the forward-looking statements contained in this annual report will, in fact, occur. Accordingly, readers should not place undue reliance on forward-looking statements. The forward-looking statements speak as of the date of this report and we do not undertake any obligation to revise or update the forward-looking statements.

STRATEGY

We have embarked on a program to increase earnings, and hence shareholder value, by improving our operating efficiency. We are seeking to grow at rates in excess of our market s general rate of growth, primarily through the introduction of qualitatively superior new products to our major marketplaces through existing customers.

INTRODUCE NEW PRODUCTS

In the last three years, we have focused our development efforts on products which address the actual technical requirements of maintaining clean air to promote health. Maintaining ultra-clean air in residential and commercial settings requires continuous and complete replacement of used air contaminated by contact with hair, skin, carpet, solvents, cigarette smoke and other common particle sources with air filtered through a combination of pre-filters, High Efficiency Particulate Air (commonly called HEPA) filtration, and odor removal, as well as controlling all air inlets. This typically requires upgraded and augmented blowers for central or zoned HVAC systems necessary to push air through more effective filters, additional filtration placed at building air inlets, and enough additional HVAC capacity to generate over-pressure so that the majority of air leaks push clean air out, rather than allow dirty air inside.

We have also been able to provide an upgrade path for government buildings, large commercial office buildings and other public venues wishing to utilize HEPA filtration as part of a program to harden buildings against bioterrorist attacks.

Most currently available air filters for commercial, industrial and residential use are primarily useful for protecting motors, coils and other mechanical components from airborne grease condensation and other contaminants which reduce the life and energy-efficiency of the HVAC equipment and have little or no effect on reducing airborne contamination which may be harmful to humans. In fact, standard pleated filters, even those with high-MERV ratings, offer no appreciable benefit in terms of better air quality for the inhabitants than the cheapest spun-glass filters. These pleated filters are accompanied by increased heating and cooling costs caused by the decreased amount of air flowing through the system, and decreased efficiency, which may be accompanied by more frequent equipment breakdowns as equipment is stressed by attempting to push higher volumes of air through tighter filters. Our new products are designed to offer end-users substantial and measurable benefits to health and productivity through substantially cleaner air, and are properly engineered to reduce detrimental effects on equipment life.

Co-branding with major name-brands. During the past four years, we have developed and co-marketed products which utilize, and are branded with, Church and Dwight's Arm&Hammer® products, and Reckit Benkiser's Lysol™. We believe the brand-name recognition associated with these products will enable us to gain entrance with major retailers who are not currently our customers or to increase the number of our products carried by current customers who only carry portions of our product line. We will continue to look for appropriately branded technologies which might produce similarly beneficial products and branding opportunities.

Security Products for Government Buildings and Commercial Office Buildings. We have adapted our containment control technology to be used in hardening government facilities, large commercial office buildings and public venues against anthrax attacks and other bioterrorist incidents. While these systems do not offer complete protection against bioterrorist attacks, any credible multi-layered defense requires HEPA filtration and related technologies adapted to the unique requirements of these facilities. Marketing for these products will include analysis and diagnostic services offered through our IAQ (Indoor Air Quality) Diagnostic Group, adapted sales literature, technical seminars and electronic multimedia presentations.

IMPROVE OPERATING EFFICIENCY

Centralize Overhead Functions. During 2003, we continued our ongoing programs to centralize functions and eliminate duplication of efforts between subsidiaries in the following areas: purchasing, production planning, shipping coordination, accounting and personnel management, risk management and benefit plan administration.

Complete Vertical and Systems Integration. During the past five years, we have continued to complete the development and redesigning of numerous systems and products which were only partially completed when we acquired the companies which originally claimed to have fully developed them. These products include the automated machinery necessary for high-speed production of our pleated filters, acquired with Precisionaire, and the mass-production processes for bonded carbon high-mass zero-density products. We have also completed systems integration efforts which were only partially in place when the companies were acquired, particularly including inventory shop-floor control, procurement oversight, and financial reporting systems at Precisionaire. We believe that complete dissemination and duplication of these products and systems throughout Flanders will result in further gains in operating efficiency and augment our bottom line.

Strategic Acquisitions. We continue to search for opportunities to acquire new businesses, although our criteria for evaluating these businesses has moved toward acquiring raw material suppliers, distributors and regional resellers, and away from acquiring competing air filter manufacturers in the United States. We will continue to search for opportunities to acquire companies in Europe and the Pacific Rim to expand our technologies in these geographic areas. We are looking for potential acquisitions with the following characteristics: (i) dominant positions in local or regional markets, (ii) a stable customer base distinct from our existing customers, and (iii) a history of consistent and healthy earnings. Acquiring resellers and distributors with these characteristics allows us to increase operating margins by removing at least one layer of middlemen, and their compounding mark-ups and commissions from the sales and distribution process, allowing us to earn higher margins while maintaining competitive pricing with end users. At the present time, we do not have any binding agreements with respect to future acquisitions.

Optimization of Mature Products. Now that we have completed the rationalization and consolidation of our product lines, we should be able to stabilize designs and complete efficiency studies on our manufacturing processes and supply chains which should enable us to duplicate our most successful processes across all plants.

INCREASE MARKET SHARE

Use Strategically Located Facilities Throughout the United States to Increase Market Share. Through acquisition and the establishment of new plants, we have placed facilities within one day s over-the-road shipping to most major population centers in the United States. We believe this ability to regionalize production and distribution has improved our business in several ways: (i) decreased cost of products to customers by reducing the average distance between our plants and both our customers and our major raw materials suppliers, hence decreasing freight expenses; (ii) increased responsiveness by decreasing the average time required to ship products to customers; and (iii) increased our share of national accounts total business by having manufacturing facilities in closer proximity to customers regional distribution centers. The ability to service all major population centers with regional manufacturing centers is critical for our business, allowing us to compete on price against less broadly based competitors without sacrificing margins as well as the ability to respond more rapidly than most of our competition.

Continued Emphasis on Quality and Performance. A continued emphasis on product quality and on-time shipments has allowed us to capture market share in serving several industries in recent years. We are expanding our NQA1 Quality Assurance Program.

Utilize High Efficiency Production and Logistics Systems to Dominate Niche Markets. During the past several years we have invested heavily in upgrading our production facilities, scheduling capacity, and logistics management capabilities. We intend to continue using these advantages to capture market share in niche markets with specialized products tailored to their exact requirements. Many end users with specialized air filtration needs are currently making do with standard products. It has been our experience that minor changes made to our standard products to meet specialized requirements may offer significant operational savings to these end users, although the actual filters cost more.

AIR FILTER MARKET BACKGROUND

The air filtration market is mature, with market growth driven by a gradual trend toward higher efficiency filters for residential, commercial and industrial applications.

According to the McIlvaine Company, a leading industry analyst, concerns about anthrax and other harmful microbes will accelerate this trend over the next five years as commercial buildings in large U.S. cities upgrade their ventilation systems to install more efficient filters. They forecast that the world market for air filters will grow to approximately $5 billion in 2005, up from $3.5 billion in 2000, with the United States being the largest market for air filters. Other growth drivers include an increasing propensity towards using higher-performance filters in commercial and residential spaces instead of current low-efficiency models, and the use of HEPA filters in new applications.

Management believes the forces driving the air filtration market are evolving, beginning in the past decade and continuing for the next several years, from preserving machinery and equipment to maintaining indoor air quality. In addition, we expect many technology industries to increase their reliance on air filters to remove microscopic and gaseous contaminants from sensitive manufacturing processes associated with semiconductor manufacturing, pharmaceutical production, ultra-pure materials manufacturing, nuclear power and materials processing, and biotechnology. Companies are devoting resources to air filtration products to enhance process efficiency and employee productivity.

Air filters are used in many different applications, including the following:

- *Commercial and Residential HVAC Systems*. Replacement filters are an essential requirement for the efficient operation of commercial and residential HVAC systems.

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Residential air cleaners. Stand-alone air cleaners which produce ultra-clean air in a defined area are also gaining in popularity among allergy sufferers and asthmatics, although follow-up sales of replacement filtration cartridges have been limited.

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General Industrial. Air filters are used in standard industrial settings to provide cleaner work environments; for example, auto makers use air filtration systems to remove oil mist contaminants from the air in their plants and industrial paint booth users utilize air filtration to remove paint particles from the air.

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Semiconductors. HEPA and carbon filters are necessary to meet the increasingly stringent manufacturing environment requirements of semiconductor manufacturers, where microscopic airborne contaminants can ruin microchips during production, having a large impact on manufacturing yield and profitability. Carbon filters are also being increasingly used to filter gaseous contaminants from semiconductor manufacturing areas.

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Pharmaceuticals. Pharmaceutical companies are increasingly using cleanrooms to prevent cross-contamination between different products and different lots of the same product being manufactured at the same facility. The increasing use of cultured microbes for drug production is also expected to increase demand for high-end containment environments.

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Biotechnology. Containment systems for the manipulation of viruses and bacteria using genetic engineering techniques are critical to the biotechnology industry.

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Nuclear Power and Materials Processing. Filtration systems are necessary to radioactive containment procedures for all nuclear facilities.

RECENT TRENDS

Recent trends in the air filter industry, as well as changes in laws and governmental regulations during the past five years, all encourage an increased awareness of the benefits of the use of air filtration products. Some of these trends and changes are:

Security Initiatives to Counter Terrorist Threats. According to the McIlvaine Company, initiatives to harden buildings against bioterrorist attacks and other security initiatives will result in many governmental and commercial facilities upgrading their HVAC systems to incorporate HEPA filters and other types of upgraded air control systems. We have seen orders decrease in this area over the past year. It would appear that some event outside the norm will need to occur to generate awareness for emergency preparedness.

Semiconductor Downturn and Economic Recovery. Sales of air filtration products for semiconductor facilities, historically a major market, are expected to be slow again during the first six months of 2004, with most analysts pushing recovery for this sector out to the third and fourth quarter of 2004. The strengthening economy is also having a positive effect on sales of all of our products.

Indoor Air Quality and Health. We believe there is an increase in public concern regarding the effects of indoor air quality on employee productivity and health, as well as an increase in interest in standards for detecting and solving IAQ problems. For example, the American Society of Heating Refrigeration and Air-Conditioning Engineers (ASHRAE) has recently established certain minimum standards for ventilation and indoor air quality for commercial and industrial settings. The World Health Organization has recently been studying the effects of air quality on human health, including widely publicized epidemiological studies indicating that airborne contaminants kill more people than automobile accidents. We are seeing a greater interest in upgrading residential filtration.

Lack of Legitimate Competing Products. We believe there is an increase in public and regulatory frustration with spurious and misleading claims made by certain manufacturers in the air filtration industry. This trend is evidenced by recent rulings by the Federal Trade Commission disallowing claims of cleaning the air in an entire room made by several manufacturers of area HEPA filtration systems as well as medical benefits claimed by manufacturers of passive electrostatic washable synthetic filters and other articles in consumer reports. We hope that as the public becomes more interested in real filtration products that we will see continued strength in this market.

Hazardous Working Environments. Several studies recognize that air quality in working facilities has an impact upon human health. OSHA regulations, in particular, have made IAQ a consideration in a wide variety of industries, ranging from those industries using spray-paint booths to those using automobile assembly lines. We are encouraged by the awareness and increased interest in improving indoor air quality in working environments.

Sick Building Syndrome. Sick Building Syndrome, which is characterized by lethargy, frequent headaches, eye irritation and fatigue, has recently been shown to be a valid concern and is a major design consideration in new and renovated commercial and industrial buildings. The identification of sick buildings, and solutions for mitigation, involve complex issues which need to be examined on a case-by-case basis by qualified engineers. Solutions typically include improving the HVAC and filtration systems of the affected buildings.

MARKETING

Much of our marketing effort consists of personal visits to customers and distributors through an extensive tiered network of contract salespeople. Periodic visits are enhanced by mass mailings announcing new products, participation in trade shows for exposure and lead generation, technical articles and advertisements in trade periodicals, and newly redesigned catalogs containing all Flanders products. During 2003 and 2004, we realigned our product offerings into groups focused on: foremarket sales, generally consisting of sales of products for new or upgraded facilities; retail sales, generally consisting of sales through retailers for use in residences and small businesses; air filter sales and service, generally consisting of sales to air filter service companies who maintain industrial and commercial HVAC systems; and after-market sales, generally consisting of sales to wholesalers and distributors for use by industrial end users; and containment sales, generally consisting of sales to government agencies or highly specialized industrial environments.

Besides developing new sales leads and contacts, we are also focused on increasing the effectiveness of our existing distributors and contract salesmen by allowing them to offer our products as a complete single-source for air filtration products.

PRODUCTS

We design, manufacture and market a broad range of air filters and related products, including:

- Residential heating and air conditioning filters, typically sold through retailers under the Flanders~Precisionaire brand name.

- Residential air cleaners, developed in 2000, which offer different filtration types ranging from single-room HEPA units which clean the air in a room to near-cleanroom levels to in-duct electrostatic precipitators which remove large quantities of airborne contaminants from entire residences without negatively impacting the efficiency of HVAC systems.

- Industrial specialty filters which fall under specifications that are categorized by efficiency ratings established by ASHRAE and used in a wide variety of industries, including paint facilities, automobile factories, chemical treatment plants, mushroom farms, coal mines, oil refineries and power plants.

- Commercial and industrial filters for use in office and general manufacturing environments, typically sold through wholesalers and distributors.

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High Efficiency Particulate Air (HEPA) filters (at least 99.97% efficient to 99.999997% efficient) in various grades, for use in semiconductor facilities, nuclear containment vessels, disease containment facilities, and other critical applications.

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Absolute Isolation Barriers which are customized stand-alone units, typically manufactured of stainless steel, used in various industries which require absolute control over contaminants, atmospheric composition and containment.

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Carbon filters, both in bonded panels, various impregnated medias, and activated charcoal beds, used to remove gaseous contaminants, odors and toxic chemical vapors in various commercial and industrial applications.

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Specialized air filter housings for use in multi-stage filtration applications.

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Other related products, including ductwork and equipment cleaning chemicals, custom air handlers and specialized filter housings.

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Paintbooth filters for any booth on the market.

MANUFACTURING

We manufacture air filters, housings, Absolute Isolation Barriers and related equipment at several facilities in the United States and Mexico, which range in size from 18,000 square feet to approximately 600,000 square feet. The major plants are:

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Nine separate manufacturing and warehousing facilities located in Washington, North Carolina; Bartow, Florida; Terrell, Texas; Salt Lake City, Utah; Momence, Illinois; Smithfield, North Carolina; Tijuana, Mexico; Stafford, Texas; and Auburn, Pennsylvania, produce a broad range of HEPA, commercial, residential and industrial filters.

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Other facilities in Bath and Washington, North Carolina, and Salt Lake City, Utah, manufacture HEGA filters, high-end containment environments, housings, custom filter assemblies and other custom filtration products and systems which require extensive custom design, production and lot tracking, including products used in the production and containment of potentially dangerous biologically engineered microorganisms.

In addition, we design and manufacture much of our automated production equipment as well as the glass-based media used in many of our products.

Our manufacturing operations are subject to periodic inspection by regulatory authorities. Because of the nature of some of our products, these agencies include the Department of Energy and other agencies responsible for overseeing sensitive technologies. One of the considerations in deciding which types of products each facility will manufacture is the segregation of highly-regulated products to a minimal number of facilities to reduce the overhead associated with regulatory monitoring and compliance.

Each of our manufacturing facilities utilizes testing and design strategies appropriate to the products manufactured. These range from standard statistical process quality controls for residential replacement filters to individual testing and certification with patented proprietary particle scanning technologies for each laminar-grade HEPA filter. We believe that our ability to comprehensively test and certify HEPA filters is a competitive advantage.

SOURCE AND AVAILABILITY OF RAW MATERIALS

Our principal raw materials are cardboard, fiberglass fibers, recyclable waste-glass, extruded glass, sheet metal, extruded aluminum, adhesives, resins and wood. All of these raw materials are readily available in sufficient quantities from many suppliers.

COMPETITION

The air filtration market is fragmented and highly competitive. There are many companies which compete in our market areas. We believe that the principal competitive factors in the air filtration business include product performance, name recognition, price, product knowledge, reputation, customized design, timely delivery and product maintenance. We believe that we compete favorably in all of these categories. Competitors include successful companies with resources, assets, financial strength and market share which may be greater than ours. Major competitors include American Air Filter International, Camfil Farr Company, Donaldson Company, Inc. and Airguard Corporation.

PATENTS, TRADEMARKS AND LICENSES

The Company and its subsidiaries currently hold twenty-seven (27) patents relating to filtration technology including patents relating to HEPA filters and fabrication methods, filter leak testing methods, filter assembly, laminar flow cleanrooms, components of isolation barriers, and the baking soda impregnation method used in the manufacture of the Arm & Hammer® infused Filters.

In addition, the Company maintains twenty-five (25) trademark registrations including the following: FLANDERS®, PRECISIONAIRE®, EZ FLOW®, SMILIE®, AIRVELOPE®, CHANNEL-CEIL®, PUREFORM®, ECONO-CELL®, GAS-PAK®, PUREFRAME®, DIMPLE PLEAT®, BLU-JEL®, VLSI®, KWIK KUT®, SUPER-FLOW®, NATURALAIRE®, AIRPURE®, PURESEAL®, FLANDERS ABSOLUTE ISOLATION®, FLANDERS/CSC®, TECH-SORB®, NATURALAIRE FILTER FRANGRANCE®, AIRIA®, and BECAUSE WE KNOW AIR FORWARDS AND BACKWARDS®. The Company also has applied for federal trademark protection for the SWISSAIRE™ mark (Serial No. 76/475,934) for its new paintbooth product line. Although management believes that the patents and trademarks associated with our various product lines and subsidiaries are valuable, we do not consider any of them to be essential to our business.

The Company currently holds a license for the intellectual property mark of Arm & Hammer® from Church & Dwight Company for labeling uses on our baking soda infused product line. The Company is party to a Royalty Agreement with Church & Dwight for the use of said mark which management believes to be a reasonable and necessary agreement that is in the best interest of the Company. Furthermore, the Company holds a license for the intellectual property mark of Lysol™ from Reckitt Benckiser, Inc. for labeling uses on our new line of antimicrobial-treated filter product line. The Company is party to a Royalty Agreement with Reckitt Benckiser for the use of the Lysol™ mark which management believes to be a reasonable and necessary agreement that is in the best interest of the Company.

CUSTOMERS

We are not dependent upon any single customer. One customer, Wal-Mart Stores, Inc., accounted for 17%, 15% and 9% of net sales during 2003, 2002 and 2001, respectively. The Home Depot, Inc., accounted for 17%, 16% and 13% of net sales during 2003, 2002 and 2001, respectively. No other single customer accounted for 10% or more of net sales during the past three years. Other significant customers include Abbott Laboratories, Motorola, Inc., Intel Corporation, Merck & Co., Inc., Upjohn Co., Westinghouse Electric Corp., and several U.S. government agencies.

BACKLOG

We had approximately $20.1 million of firm backlog on December 31, 2003, compared to $12.2 million on December 31, 2002. Firm backlog includes orders received and not yet begun and the unfinished, unbilled portion of special orders. Orders are typically not cancelable without penalty, except for certain stable filter supply contracts to nuclear facilities operated by the United States government. Backlog varies from week to week, based on the timing and mix of orders received. The difference in backlog between December 31, 2003 and 2002 is not considered to be meaningful, and is within the normal range of week-to-week variation. All backlog at December 31, 2003, is expected to be shipped by the end of the second quarter of 2004.

EMPLOYEES

The Company employed 2,166 full-time employees on December 31, 2003; 1,800 in manufacturing, 42 in development and technical staff, 28 in sales and marketing, and the remaining 296 in support staff and administration. The Company believes that its relationship with its employees is satisfactory.

GOVERNMENT REGULATION

Although we believe our operations are in material compliance with applicable environmental laws and regulations, risks of significant costs and liabilities are inherent in manufacturing operations, and we cannot assure that significant costs and liabilities will not be incurred. Moreover, it is possible that other developments, such an increasingly strict environmental laws and regulations and enforcement policies thereunder, and claims for damages to property or persons resulting from our operations, could result in substantial costs and liabilities to us. We believe that changes in environmental laws and regulations will not have a material adverse effect on our financial position, results of operations or cash flows in the near term.

We are also subject to the requirements of OSHA and comparable state statutes. We believe we are in material compliance with OSHA and state requirements, including general industry standards, record keeping requirements and monitoring of occupational exposures. In general, we expect to increase our expenditures to comply with stricter industry and regulatory safety standards such as those described above. Although such expenditures cannot be accurately estimated at this time, we do not believe that they will have future material adverse effect on our financial position, results of operations or cash flows.

SEASONALITY

Historically, our business has been seasonal, with a substantial percentage of sales occurring during the second and third quarters of each year. In addition, demand for our general commercial and industrial products appears to be highly influenced by the weather, with higher sales generally associated with extremes of either hot or cold weather, and lower sales generally associated with temperate weather. Because of these seasonal and weather-related demand fluctuations, quarter-to-quarter performance may not be a good predictor of future results.

EXPORT SALES

We sell products to end users outside of the United States through domestic specialty cleanroom contractors. These sales are counted as domestic sales. We also sell products through foreign distributors, primarily in Europe, and through Flanders International, Ltd., a wholly-owned subsidiary located in Singapore which sells to customers in the Pacific Rim. Sales through foreign distributors and Flanders International amounted to less than 5% of net sales for each of the last three fiscal years. Assets held outside the United States are negligible.

Item 2.

Properties

The following table lists our principal facilities. Management believes that these properties are adequate for its current operational needs. We may, at some point, relocate, reorganize or consolidate various facilities for reasons of operating efficiencies or may open new plants to take advantage of perceived new economic opportunities. We are of the opinion that all properties are well maintained and appropriately insured.

Principal Facility	Location	Approximate Floor Space (sq. ft.)	Monthly Payment	Lease/Type
Manufacturing and office facility	Washington, North Carolina	285,000	N/A	Owned
Manufacturing, service and office facility	Bath, North Carolina	46,000	N/A	Owned
Manufacturing plant	Bartow, Florida	175,000	N/A	Owned
Warehouse	Bartow, Florida	60,000	$15,598	Leased
Manufacturing plant	Terrell, Texas	168,000	$23,562[1]	Owned
Manufacturing plant	Auburn, Pennsylvania	92,000	$6,125[1]	Owned
Office space and headquarters	St. Petersburg, Florida	18,000	N/A	Owned

Principal Facility	Location	Approximate Floor Space (sq. ft.)	Monthly Payment	Lease/Type
Manufacturing plant	Momence, Illinois	211,000	$135,353[1]	Owned

Sales office and warehouse	Singapore	3,800	$2,100	Leased
Manufacturing and warehouse	Smithfield, North Carolina	415,000	$62,924	Leased[1]
Manufacturing plant	Smithfield, North Carolina	474,000	$6,173[1]	Owned
Manufacturing and office facility	Stafford, Texas	18,000	N/A	Owned
Manufacturing plant	Salt Lake City, Utah	192,000	N/A	Owned
Manufacturing plant and office facility	San Diego, California	96,000	$48,226	Leased
Manufacturing plant	Tijuana, Mexico	127,000[1]	$44,000	Leased
Direct Sales Office	Phoenix, Arizona	22,000	$8,742	Leased
Direct Sales Office	Santa Fe Springs, California	20,000	$11,514	Leased
Direct Sales Office	Hayward, California	10,000	$6,500	Leased
Direct Sales Office	Salt Lake City, Utah	15,000	$3,000	Leased
Direct Sales Office	Sanford, North Carolina	1,000	$950	Leased
Direct Sales Office & Warehouse	Kent, Washington	12,500	$7,000	Leased

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Item 3.

Legal Proceedings

We are involved in a dispute with a benefit plan administrator (U.S. District Court, Middle District of Florida, Tampa Division, Case No. CIV 1971-T-17-F, Liberty Mutual v. Flanders Corporation et al). Liberty Mutual was the Workers Compensation administrator and stop-loss insurer for some of the Company s subsidiaries. They have alleged that they are entitled to be reimbursed for certain costs incurred in administering various insurance claims. We have counter-sued, claiming that Liberty Mutual has acted in bad faith, was negligent in its duties as administrator of our claims, that it made payments on our behalf which were specifically disallowed, that they refused to follow instructions given to them by us, that they failed to meet minimal acceptable standards for administering claims, and that such failures constituted a material dereliction of their responsibilities as administrator, as well as other claims related to malfeasance and negligence. In addition, we claimed Liberty Mutual charged certain administrative fees over and above the actual costs incurred. The amount and probability of any settlement or award related to this litigation is unknown at this time. Among the issues being considered is the matter of currently unresolved workers compensation claims whose estimate of potential loss may change as a result of this litigation. While management believes it has reserved an adequate amount for settlement of these claims, there is no guarantee that the Company s actual liability will not exceed its current estimate. Accordingly, these matters, if resolved in a manner different from management s estimate, could have a material effect on the operating results or cash flows in the future.

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

Additionally, from time to time, we are a party to various legal proceedings incidental to our business. None of these proceedings are material to our business, operations or financial condition.

In the opinion of the Company, although the outcome of any legal proceeding cannot be predicted with certainty, the ultimate liability of the Company in connection with currently known legal proceedings will not have a material adverse effect on the Company s overall financial position, but could be material to the results of operations for a particular period in the future.

Item 4.

Submission of Matters to a Vote of Security Holders

The Company held its annual meeting of shareholders on December 19, 2003. During the meeting, holders of 22,859,390 shares, representing eighty-eight percent (88%) of the 26,083,846 shares outstanding on the record date, attended either in person or by proxy. Holders of 22,597,673 shares (approximately 87% of those shares present) cast votes for the election of members to the Board of Directors for Robert R. Amerson, Steven K. Clark, D. Michael Steele, David M. Mock, and Peter Fredericks. Holders of 755,728 shares chose to withhold their votes for directors. As a result of the meeting, Messrs. Amerson, Clark, Steele, Mock, and Fredericks were elected for an additional one-year term as directors.

PART II

Item 5.

Market for Registrant s Common Equity and Related Stockholder Matters

PRICE RANGE OF COMMON STOCK

The Company s common stock is listed on the Nasdaq National Market System under the symbol FLDR. The following table sets forth, for the periods indicated, the high and low sale prices of the Company s common stock as reported by the Nasdaq National Market System. Such quotations do not include retail mark-ups, mark-downs, or other fees or commissions.

	High	Low
2003		
Fourth Quarter ended December 31, 2003	$ 7.01	$ 4.45
Third Quarter ended September 30, 2003	$ 6.05	$ 2.71
Second Quarter ended June 30, 2003	$ 2.95	$ 2.09
First Quarter ended March 31, 2003	$ 2.23	$ 1.43
2002		
Fourth Quarter ended December 31, 2002	$ 1.88	$ 1.42
Third Quarter ended September 30, 2002	$ 1.88	$ 1.45
Second Quarter ended June 30, 2002	$ 2.03	$ 1.44
First Quarter ended March 31, 2002	$ 2.49	$ 1.70

2001		
Fourth Quarter ended December 31, 2001	$ 2.72	$ 1.56
Third Quarter ended September 30, 2001	$ 2.45	$ 1.61
Second Quarter ended June 30, 2001	$ 2.15	$ 1.16
First Quarter ended March 31, 2001	$ 3.69	$ 1.30

EQUITY COMPENSATION PLAN INFORMATION

The following table provides information about our Equity Compensation Plans.

Plan Category	Number of securities to be issued upon exercise of outstanding options	Weighted average price of outstanding options	Number of securities remaining available for future issuance
Long Term Incentive plan approved by security holders	265,000	$3.08	1,493,000
Long Term Incentive plan not approved by security holders	-	-	-
Directors and Officers plan approved by security holders	270,000	$2.62	170,000
Directors and Officers plan not approved by security holders	-	-	-
Other equity compensation plan approved by security holders	4,000,000	$5.00	-
Other equity compensation plan not approved by security holders	-	-	-

APPROXIMATE NUMBER OF EQUITY SECURITYHOLDERS

On February 20, 2004, Flanders’ common stock closed at $5.91. As of February 20, 2004, there were approximately 155 holders of record of the Company s common stock. The Company estimates there are approximately 6 beneficial owners (holders of more than 5% of the common stock) of the Company s common stock.

DIVIDENDS

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

SALES OF UNREGISTERED SECURITIES

The Company did not sell any unregistered securities during 2003, 2002 or 2001.

Item 6.

Selected Financial Data

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

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

	Year Ended December 31,				
	2003	2002	2001	2000	1999
	$	$	$	$	$
Net sales	182,780	184,211	189,077	194,072	171,392
Gross profit	43,271	40,821	39,782	36,917	43,975
Operating expenses	32,112	29,591	36,311	40,733	33,802
Operating income (loss) from continuing operations	11,159	11,230	3,471	(3,816)	10,172

Earnings (loss) from continuing operations before income taxes	11,251	7,740	1,489	(6,940)	10,174
Provision (benefit) for income taxes	3,505	3,001	930	(2,443)	4,671
Earnings (loss) from continuing operations	7,746	4,739	559	(4,497)	5,503
Loss from discontinued operations			(175)	(2,702)	(2,686)
Cumulative effect of accounting change		(27,681)			
Net earnings (loss)	7,746	$ (22,942)	$ 384	$ (7,199)	$ 2,817
Earnings (loss) per share from continuing operations					
Basic	$ 0.30	$ 0.18	$ 0.02	$ (0.18)	$ 0.22
Diluted	$ 0.29	$ 0.18	$ 0.02	$ (0.18)	$ 0.21
Net earnings (loss) per share					
Basic	$ 0.30	$ (.88)	$ 0.01	$ (0.28)	$ 0.11
Diluted	$ 0.29	$ (.88)	$ 0.01	$ (0.28)	$ 0.11
Weighted average common shares outstanding					
Basic	26,033	26,033	26,036	25,298	25,344
Diluted	26,428	26,033	26,038	25,298	26,525

SELECTED HISTORICAL BALANCE SHEET DATA (In thousands)

	December 31,				
	2003	2002	2001	2000	1999
Working capital	$ 45,547	$ 41,389	$ 14,603	$ 13,644	$ 45,421
Total assets	145,415	141,671	180,255	180,222	165,642
Long-term obligations[1]	26,290	35,475	52,045	49,370	32,328
Total shareholders equity	80,709	72,928	96,879	98,151	107,817

1

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

Item 7.

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

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

OVERVIEW

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

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

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

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

We value our inventories at the lower of cost or market. We write down inventory balances for estimated obsolescence or unmarketable inventory equal to the difference between the cost of the inventory and the estimated market value based upon assumptions about future demand and market conditions. If actual market conditions are less favorable than those projected by management, additional inventory write-downs may be required.

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

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

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

The change in the carrying amount of goodwill and other intangibles (net of accumulated amortization) for the year ended December 31, 2003 is as follows:

Balance at December 31, 2001	$	27,681
Transitional goodwill impairment loss		(26,933)
Transitional other intangible impairment loss		(748)
Total transitional impairment loss		(27,681)
Balance at December 31, 2002	$	-
Balance at December 31, 2003	$	-

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

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

2003 Compared to 2002

The following table summarizes the Company s results of operations as a percentage of net sales for 2003 and 2002.

	2003		2002	
Net sales	$ 182,780	100.0%	$ 184,211	100.0%
Gross profit	43,271	23.7	40,821	22.2
Operating expenses	32,112	17.6	29,591	16.1
Operating income	11,159	6.1	11,230	6.1
Nonoperating income (expense)	92	.1	(3,490)	(1.9)
Earnings before income taxes	11,251	6.2	7,740	4.2
Provision for income taxes	3,505	1.9	3,001	1.6
Earnings before cumulative effect of a change in accounting principles	7,746	4.2	4,739	2.6
Cumulative effect of accounting change	-	0.0	(27,681)	(15.0)

Net earnings (loss)	$ 7,746	4.2	$ (22,942)	(12.5)

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

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

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

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

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

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

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

2002 Compared to 2001

The following table summarizes the Company s results of operations as a percentage of net sales for 2002 and 2001 (dollar amounts in thousands).

	2002		2001	
Net sales	$ 184,211	100.0%	$ 189,077	100.0%
Gross profit	40,821	22.2	39,782	21.0
Operating expenses	29,591	16.1	36,311	19.2
Operating income (loss) from continuing operations	11,230	6.1	3,471	1.8
Nonoperating income (expense) from continuing operations..	(3,490)	(1.9)	(1,982)	(1.0)
Earnings (loss) from continuing operations before income taxes	7,740	4.2	1,489	0.8
Provision (benefit) for income taxes	3,001	1.6	930	0.5
Earnings (loss) from continuing operations	4,739	2.6	559	0.3
Cumulative effect of accounting change	(27,681)	(15.0)	-	0.0
Net earnings (loss)	$ (22,942)	(12.5)	$ 384	0.2

Net Sales: Net sales for 2002 decreased by $4,866 or 2.6%, to $184,211, from $189,077 for 2001. The decrease in net sales was due to a general decrease in air filter sales across the industry which began in the fourth quarter of 2001 and the elimination of unprofitable product lines, partially balanced by our success in increasing our market share, particularly among national retailers.

Gross Profit: Gross profit for 2002 increased $1,039, or 2.6%, to $40,821, which made up 22.2% of net sales, from $39,782 for 2001, which made up 21.0% of net sales. The gross profit increase was principally attributable to:

- Expanded facilities in Tijuana, which were brought fully online and stabilized during the first half of 2002, resulting in savings in rent, taxes and labor-related costs.

- Reductions in raw material expenses due to in-house production of spun-glass.

-

Reductions in direct labor force headcount.

Operating Expenses: Operating expenses for 2002 decreased $6,720, or 18.5%, to $29,591, from $36,311 in 2001. The decrease in operating expenses was caused by a decrease of $798 of amortization of goodwill expenses caused by our adoption of SFAS 142 effective January 1, 2002. The remainder of this decrease was primarily attributable to reductions in administrative salaries, benefits of centralized shipping control, improved scheduling and renegotiated shipping terms.

Nonoperating income (expense) from continuing operations: Nonoperating expenses from continuing operations increased approximately $1,508, or 76%, to a net expense of approximately $3,490 for 2002, compared to net expense of $1,982 in 2001. The increase was primarily an increase in interest expenses and fees associated with our former credit line with SunTrust Bank, N.A. See Liquidity and Capital Resources below.

Provision for Income Taxes: Our effective state and federal tax rate, adjusted for the effect of nondeductible expenses consisting primarily of amortization of goodwill of $798 in 2001, was approximately 39% and 39% for 2002 and 2001, respectively.

Earnings from Continuing Operations: Earnings from continuing operations for 2002 increased $4,180, to $4,739, or $0.18 per share, from $559, or $0.02 per share for 2001. The increase in earnings is primarily attributable to realized production efficiency gains, administrative savings and reductions in salary expense.

EFFECTS OF INFLATION

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

LIQUIDITY AND CAPITAL RESOURCES (dollar amounts in thousands)

Working capital was $45,547 at December 31, 2003, compared to $41,389 at December 31, 2002. This included cash and cash equivalents of $1,098 and $2,806 at December 31, 2003 and 2002, respectively. The primary reason for the increase in working capital was cash flows generated from operations net of amounts used to reduce debt by approximately $9,000.

Trade receivables increased $1,877, or 5.5% at December 31, 2003 from $34,031 at December 31, 2002. The increase in accounts receivable at the end of 2003 is attributable to increased aging of various accounts along with the timing differences in shipments and payments received.

Continuing operations generated $12,313 of cash in 2003, compared to $16,624 of cash in 2002. The difference in cash flows was primarily related to increases in inventory and receivables partially offset by higher operating income. Investing activities for continuing operations consumed $5,010 of cash during 2003, compared to generating $84 during 2002, consisting primarily of the purchase of property and equipment, balanced by the sale of assets, including the sale of direct sales offices in the Tidewater Group in 2002. Financing activities for continuing operations consumed $9,011 of cash in 2003, consisting primarily of payments on long-term debt, compared to consuming $17,780 of cash in 2002, consisting primarily of payments on long-term debt.

On October 17, 2002, we signed agreements for a new credit facility with Fleet Capital Corporation, which replaced and repaid our previous $30 million revolving credit facility. The new $40 million facility consists of a $7 million term loan and a $33 million revolving credit line, both of which expire on October 17, 2007. The term loan bears interest, at our option, at either (i) LIBOR plus between 2.5% and 3%, dependent on the Company s fixed charge coverage during the prior twelve months; or (ii) the greater of the Federal Funds Effective Rate plus 0.5% or Fleet s base rate, plus between 0.5% and 1%, dependent on the Company s fixed charge coverage during the prior twelve months. The $33 million revolving credit facility bears interest at 0.25% less than the term loan. Up to $11 million of the revolving credit facility may be used to issue letters of credit. The facility is collateralized by substantially all of the Company s assets. The line of credit agreement requires maintenance of certain financial ratios, and restricts capital expenditures, dividends and share repurchases. Unless this credit facility is renewed, it will expire on October 17, 2007. There are no prepayment penalties on any of the credit facilities with Fleet Capital Corporation.

In connection with the amended working capital credit facility and notes payable to a regional development authority and bank, the Company has agreed to certain restrictive covenants which include, among other things, restricting capital expenditures to less than $6,250 for 2003 and $3,250 per year, thereafter, not paying dividends or repurchasing its stock without prior written consent, and maintenance of certain financial ratios at all times including: a minimum current ratio, minimum tangible net worth, a maximum ratio of total liabilities to tangible net worth and a minimum fixed charge coverage ratio.

As of December 31, 2003 we had the following fixed obligations and commitments:

				Other long-term obligations
Year ended December 31,	**Operating leases**	**Capital leases**	**Long-term debt**	
2004	2,315	467	2,075	

2005	1,799	436	2,104	
2006	826	465	1,886	
2007	342	527	1,634	
2008	145	522	1,942	
Thereafter	249	856	13,376	1,850

We believe that our cash on hand, cash generated by operations, and cash available from our existing credit facilities is sufficient to meet the capital demands of our current operations during the 2004 fiscal year. Any major increases in sales, particularly in new products, may require substantial capital investment for the manufacture of filtration products. Failure to obtain sufficient capital could materially adversely impact our growth potential.

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

In 1998, the Board of Directors authorized the repurchase of up to two million shares of our common stock, which repurchase was completed in September 2000. On September 22, 2000, the Board of Directors authorized the repurchase of up to an additional two million shares of common stock through open market or negotiated transactions. Further repurchases under this program are restricted under our current line of credit agreement, and require prior consent of Fleet Capital Corporation. As of February 23, 2004, approximately 575,000 shares had been repurchased in the open market under this authorization.

Outlook

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

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

We have adapted our biocontainment products for use as part of a system for hardening government buildings, commercial office complexes and public venues against airborne bioweapons such as anthrax and smallpox. There is currently a decline of interest in these products, and major market analysts have indicated this will continue, until some significant event occurs to once again trigger an interest in emergency preparedness. Any interest towards hardening these types of facilities against airborne bioweapons could have a significant impact on our business.

Sales of air filtration products for semiconductor facilities, historically a major market, are expected to be slow again during the first six months of 2004, with most analysts pushing recovery for this sector out to at least the third or fourth quarter 2004. The current economy is also expected to have a dampening effect on sales of air filtration products across all product lines and end-user categories. As long as the current weakness in the economy continues, in individual market segments or the marketplace as a whole, our results will be negatively affected.

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

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

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

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

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

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

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

Factors That May Affect Future Results

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

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

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

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

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

During 2004 and 2005, we plan to introduce and market various products which, if successful, may require additional financing and/or capital. This financing may need to be available on short notice. Any failure to obtain such financing, or delay in financing, could cause the failure of the new products due to inability to deliver on time, and could adversely impact relationships with current major accounts. In addition, delays in an untried supply chain, new production chains, and other delays common to the launch of a new product line could also adversely impact the success of the products, as well as current relationships with major accounts.

Our Business May Suffer If Our Competitive Strategy is Not Successful

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Management Controls a Significant Percentage of Our Stock

As of February 23, 2004, our directors and executive officers beneficially held approximately 49.98% of our outstanding common stock. As a result, such shareholders effectively control or significantly influence all matters requiring shareholder approval. These matters include the election of directors and approval of significant corporate transactions. Such concentration of ownership may also have the effect of delaying or preventing a change in control that may otherwise be advantageous to the non-affiliated shareholders.

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

We have granted options to purchase a total of 4,535,000 shares of common stock to various parties with exercise prices ranging from $1.50 to $7.50 per share. The majority of these options are currently exercisable. Additionally, if the option holders exercise their options, the interests of current shareholders may be diluted.

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

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

Our Business Can be Significantly Affected by Environmental Laws

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

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

Item 7A.

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

We are exposed to various market risks, primarily changes in interest rates. Market risk is the potential loss arising from adverse change in market rates and prices, such as foreign currency exchange and interest rates. For Flanders, these exposures are primarily related to changes in interest rates. We do not hold any derivatives or other financial instruments for trading or speculative purposes.

The fair value of the Company s total long-term debt, including capital leases and current maturities of long-term debt, at December 31, 2003 was $26,290. Market risk was estimated as the potential decrease (increase) in future earnings and cash flows resulting from a hypothetical 10% increase (decrease) in the Company s estimated weighted average borrowing rate at December 31, 2003. Although most of the interest on the Company s debt is indexed to a market rate, there would be no material effect on the future earnings or cash flows related to the Company s total debt for such a hypothetical change.

We have only a limited involvement with derivative financial instruments. We have two interest-rate swap agreements to hedge against the potential impact on earnings from increases in market interest rates of two variable rate bonds. Under the interest rate swap agreements, we receive or make payments on a monthly basis, based on the differential between 5.14% and a tax exempt interest rate as determined by a remarketing agent. This interest rate swap is accounted for as a cash flow hedge in accordance with SFAS 133 and SFAS 138. Gains or losses related to inefficiencies of the cash flow hedge were included in net income during the period related to hedge ineffectiveness. The tax affected fair market value of the interest rate swap of $1,110 is included in Accumulated other comprehensive loss on the balance sheet. The interest rate swap contracts expire in 2013 and 2015.

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

Item 8.

Financial Statements and Supplementary Data

Beginning at page F-1.

Item 9.

Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

On December 9, 2002, the Audit Committee of Flanders Corporation (i) approved the engagement of Pender Newkirk & Company, CPAs, as the independent accountants for Flanders Corporation and (ii) accepted the resignation of Grant Thornton as such independent accountants. The Company had been reviewing whether to continue the relationship with Grant Thornton, and by letter dated December 6, 2002 to the Company, Grant Thornton confirmed their resignation.

The accountants report of Grant Thornton on the consolidated financial statements of Flanders Corporation and subsidiaries as of and for the years ended December 31, 2001 and 2000 did not contain any adverse opinion or disclaimer of opinion, and was not qualified or modified as to uncertainty, audit scope, or accounting principles.

The following matters represent disagreements required to be reported in accordance with Item 304 of Regulation S-K, all of which were resolved to Grant Thornton s satisfaction:

In its letter sent to the audit committee of the Company in connection with the audit for the year ended December 31, 2000, Grant Thornton indicated that it disagreed with the Company s levels of allowance for doubtful accounts and allowance for inventory.

Grant Thornton disagreed with the Company about whether or not their review of the financial information contained in the Form 10-Q for the quarter ended June 30, 2002 had been completed prior to the original filing of the Form 10-Q on August 19, 2002.

Grant Thornton disagreed with the Company over disclosures in the Company s originally filed Form 10-Q for the quarter ended June 30, 2002, contained in Footnote A Nature of Business and Interim Financial Statements regarding the completion of the first step of the transitional impairment test required by Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets.

During the Company s two most recent fiscal years and interim periods preceding resignation, Grant Thornton did not advise management or the Board of Directors of the Company of any issues regarding significant internal control matters, problems with management representations, requirements for expanded audit scope or information that materially impacts the fairness or reliability of the Company s financial statements and, accordingly, there were no reportable events.

During the past two years, Pender Newkirk & Company has not advised the Company regarding any reportable event as defined in Item 304 (a)(1)(v) of Regulation S-K.

Item 9A.

Controls and Procedures

Under the supervision and with the participation of management, including the CEO and CFO, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act), as of December 31, 2003. Based on this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures are effective.

In particular, we evaluated our inventory accounting procedures and developed additional accounting control processes related to these transactions to ensure they are recorded timely and accurately in the financial statements. We also developed, and are currently implementing, new processes and procedures to ensure that our reports under the Exchange Act are completed in a timely and accurate manner.

PART III

Item 10.

Directors and Executive Officers of the Registrant

IDENTIFICATION OF DIRECTORS AND EXECUTIVE OFFICERS

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

Name	Age	Title
Robert R. Amerson	52	President, Chief Executive Officer and Director
Steven K. Clark	50	Chief Operating Officer, Vice President Finance/Chief Financial Officer and Director
James L. Buddy Mercer	60	Vice President Operations

Peter Fredericks

45

Independent Director

D. Michael Steele

48

Independent Director

David M. Mock

51

Independent Director

Robert R. Amerson. Mr. Amerson has been President and Chief Executive Officer since 1988. Mr. Amerson is also a Director, a position he has held since 1988. He initially joined the Company in 1987 as Chief Financial Officer. Mr. Amerson has a Bachelor of Science degree in Business Administration from Atlantic Christian College.

Steven K. Clark. Mr. Clark was named as Vice President Finance, Chief Financial Officer and Director in December 1995 and Chief Operating Officer in November 1999. Mr. Clark acted as a consultant from November, 1995 through December, 1995. From July 1992 through October 1995, he was the Chief Financial Officer of Daw Technologies, Inc., a specialty cleanroom contractor and customer of the Company. Prior to this he was a senior partner of Miller and Clark, an accounting and management services firm. Mr. Clark spent four years with Price Waterhouse, and an additional four years with Arthur Andersen, both accounting firms. He is a Certified Public Accountant, has Bachelor of Arts degrees in Accounting and Political Science and a Master of Business Administration Degree, all from the University of Utah.

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

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

Economics and Business Administration.

D. Michael Steele. Mr. Steele was elected as a Director in December 2002. Mr. Steele is a partner in The Insurance Group, an insurance brokerage, and serves on the Board of Directors of the City of Greenville Airport Authority, the Pitt County North Carolina Special Olympics and the Pitt County Boys and Girls Club. Mr. Steele received his Bachelor of Science degree from Purdue University, and his Masters Degree from Bowling Green State University.

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

Item 11.

Executive Compensation

SUMMARY COMPENSATION TABLE

The following table sets forth the aggregate cash compensation paid by the Company for services rendered during the last three years to the Company s Chief Executive Officer and to each of the Company s other executive officers whose annual salary, bonus and other compensation exceeded $100,000 in 2003.

Annual Compensation		Long-Term Compensation		
		Awards		Payouts
	Other Annual Compen-	Restricted Stock Award(s)	Securities Underlying Options/ SARs	LTIP Payouts

Name and Principal Position	Year	Salary ($)	Bonus ($)	sation ($)	($)	(#)	($)
		$	$	$	$	$	$
Robert R. Amerson	2003	250,000		2,596			
					$		$
President and CEO	2002[1]	249,039		1,231			
	2001	241,347		10,500		1,000,000	
James L. Buddy Mercer	2003	120,521				80,000	
Vice President Operations	2002	112,608					
	2001	110,952					
Steven K. Clark	2003	254,808		1,587			
Vice President Finance/CFO	2002[1]	249,519		1,348			
	2001	240,866		1,327		1,000,000	

1

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

AGGREGATED OPTION/SAR EXERCISES IN LAST FISCAL YEAR

AND FISCAL YEAR-END OPTION/SAR VALUES

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

Name	Shares Acquired On Exercise (#)	Value Realized ($)	Number of Securities Underlying Unexercised Options/SARs at Fiscal Year-End (#) Exercisable/Unexercisable	Value of Unexercised In-the-Money Options/ SARs at Fiscal Year-End Exercisable/Unexercisable
Robert R. Amerson		$	2,000,000 /	4,080,000 /
James L. Buddy Mercer		$	80,000 /	275,200 /
Steven K. Clark		$	2,000,000 /	4,080,000 /

COMPENSATION OF DIRECTORS

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

EMPLOYMENT AGREEMENTS

Messrs. Amerson and Clark have employment agreements effective as of December 15, 1995 (Employment Agreements). The Employment Agreements, as amended, provide for an annual base salary of $250,000 for both Mr. Amerson and Mr. Clark and terminate in 2010. The Employment Agreements als