FLANDERS CORP
Form 10-K/A
September 15, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A
AMENDMENT NO.3

(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, 2005

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)

Registrant s 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 _√_ 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 registrant s 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 _√_

As of June 30 , 200 5, the aggregate market value of the voting stock held by non-affiliates of the registrant was approximately $158.6 million.

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

YES √

NO _

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

YES___

NO _√_

As of February 20, 2006, the number of shares outstanding of the registrant s common stock was 26,340,408 shares.

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

Explanatory Note:
This amendment on Form 10-K/A Amendment No.2 includes Exhibit 31 - Certification 302 of the Sarbanes-Oxley Act of 2002 and Exhibit 32 – Certification 906 of the Sarbanes-Oxley Act of 2002. The Form 10-K/A Amendment No.2 did not include these certifications. All other information contained in this Annual Report on Form 10-K/A Amendment No.2 is as of the date of the original filing.

FLANDERS CORPORATION

FORM 10-K

FOR THE YEAR ENDED DECEMBER 31, 2005

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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, pharmaceuticals, chemical, biological, radiological and nuclear processing. 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, chemical, biological, radiological 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 33713. 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 developed 5 new patents associated with our new nested filter concept during 2005. This concept will enable us to stack 4 filters into a space normally holding only 1 filter. This will provide labor savings associated with handling of inventory, storage space savings as well as significant freight savings. We expect to roll this product out into retail stores during the first quarter of 2006.

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 2005, 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. Additionally, the glass technology previously purchased, was not as developed as the seller had represented, resulting in significant additional cost to develop this technology and the machines are still not producing at promised run rates We are currently trying to address this issue which may require an additional acquisition or the expenditures of additional resources to meet or reach expected results. 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. During 200 6 , we are planning to move from semi automated lines to fully automated production lines which is expected to significantly reduce our labor related costs and complete our vertical integration by acquisition of additional filter media manufacturing companies.

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

Additionally, during 2004, Flanders Complete Service Division (Flanders CSD), an air filtration service provider was formed. Flanders CSD will offer weekly, monthly and quarterly service contracts for clean room and glove box certification; commercial, industrial, retail and residential surveys; and complete filtration management including mold remediation and analysis. The company is currently negotiating several large contracts and if they are executed, the company expects to have national coverage by the end of 2006.

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. However, we are currently considering the acquisition of a glass mat producer which would reduce our glass material cost and enable us to avoid the additional development costs to develop the glass technology that was previously purchased. Additionally, we are considering the acquisition of a trucking company that would enable us to reduce our transportation costs which are a significant cost of the filter industry. We are evaluating various air filter sales and

service organizations that may help us enter new markets that we do not currently enjoy.

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. We will continue to review the market for new locations for expansion.

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.

Management is of the belief that 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 and or facilitating 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:

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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, containment systems are necessary to provide shielding.

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Chemical, Biological and Radiological Safe Environments. Filtration systems are necessary to provide a safe environment for those working in sensitive areas that may be subject to exposure to such substances.

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. We believe, 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 increase in this area over the past quarter.

Semiconductor Downturn and Economic Recovery. Sales of air filtration products for semiconductor facilities, historically a major market, are expected to be slow again during 2006, with most analysts pushing recovery for this sector out until 2007. 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 systems as well as commercial systems to address both energy savings and better indoor quality.

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 2004, we realigned our product offerings into groups focused on: foremarket high purity 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.

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

Additionally, during 2004, Flanders Complete Service Division (Flanders CSD), an air filtration service provider was formed. Flanders CSD will offer weekly, monthly and quarterly service contracts for clean room and glove box certification; commercial, industrial, retail and residential surveys; and complete filtration management including mold remediation and analysis. The company is currently negotiating several large contracts and if they are executed, the company expects to have national coverage by the end of 2006..

PRODUCTS

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

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

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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.

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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.

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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.

•

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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Surface finishing filters for any paint booth or surface finishing application in the overall surface finishing 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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Ten separate manufacturing and warehousing facilities located in Washington, North Carolina (2 plants) ; 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, Salt Lake City, Utah, and Stafford, Texas, 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.

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Fifteen direct offices spread across the US that provide a distribution point as well as light manufacturing.

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, Department of Defense 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, stainless steel, various grades of mild rolled steel, 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 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 holds approximately (30) Thirty 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 developed 5 new patents associated with its new nested filter concept during 2005. This concept will enable us to stack 4 filters into a space normally holding only 1 filter. This will provide labor savings associated with handling of inventory, storage space savings as well as significant freight savings. We expect to roll this product out into retail stores during the first quarter of 2006.

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 15%, 15% and 17% of net sales during 2005, 2004 and 2003, respectively. The Home Depot, Inc., accounted for 15%, 16% and 17%

of net sales during 2005, 2004 and 2003, 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 $26.0 million of firm backlog on December 31, 2005, compared to $25.9 million on December 31, 2004. 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, 2005 and 2004 is not considered to be meaningful, and is within the normal range of week-to-week variation. All backlog at December 31, 2005, is expected to be shipped by the end of the second quarter of 2006.

EMPLOYEES

The Company employed 2,743 full-time employees on December 31, 2005; 2,463 in manufacturing, 19 in development and technical staff, 79 in sales and marketing, and the remaining 182 in support staff and administration. None of these are represented by a union. 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, 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. However, during 2005 we have begun to see a potential change in this historical pattern. We believe that increased energy costs have encouraged not only the home owner, but industrial and commercial operations to begin to realize the benefits of timely filter replacement. This resulted in higher than usual fourth quarter sales. We believe that this will continue in future years. 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	Monthly	Lease/Type

		Space (sq. ft.)	Payment	
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	$15,671	Leased
Manufacturing plant	Terrell, Texas	168,000	$23,980[1]	Owned
Manufacturing plant	Auburn, Pennsylvania	92,000	$5,857[2]	Owned
Office space and headquarters	St. Petersburg, Florida	18,000	N/A	Owned
Manufacturing plant	Momence, Illinois	211,000	$135,584 [3]	Owned
Sales office and warehouse	Singapore	3,800	$2,100	Leased
Manufacturing and warehouse	Smithfield, North Carolina	415,000	$79,816	Leased[4]
Manufacturing plant	Smithfield, North Carolina	474,000	$11,981[5]	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	$49,914	Leased
Manufacturing plant	Tijuana, Mexico	127,000[6]	$46,651	Leased
Direct Sales Office	Phoenix, Arizona	22,000	$6,697	Leased
Direct Sales Office	Santa Fe Springs, California	20,000	$8,650	Leased
Direct Sales Office	Hayward, California	10,000	$5,900	Leased
Direct Sales Office	Salt Lake City, Utah	15,000	$3,139	Leased
Direct Sales Office	Sanford, North Carolina	1,000	$950	Leased
Direct Sales Office & Warehouse	Kent, Washington	12,500	$5,640	Leased
Manufacturing plant	Washington,North Carolina	110,000	12,500	Leased
	Philadephia, Pennsylvania	26,000	16,000	Leased

Direct Sales Office & Warehouse				
Direct Sales Office & Warehouse	Cerritos, California	21,735	11,270	Leased
Direct Sales Office & Warehouse	Tucker, Georgia	34,600	16,000	Leased
Direct Sales Office & Warehouse	Raleigh, North Carolina	24,000	14,000	Leased
Direct Sales Office & Warehouse	Las Vegas, Nevada	10,106	8,006	Leased

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1Property encumbered by a mortgage on which monthly payments are made.

2Property encumbered by a mortgage on which monthly payments are made.

3Property is pledged as security for an Economic Development Revenue Bond with a face value of $6,000,000. The obligation is paid quarterly rather than monthly by paying a portion of principal and interest on the entire amount. The payment shown above is for the entire fourth quarter of 2005.

4The property and building is owned by a partnership consisting of two of the Company's officers and directors.

5The property is used as security for a two Industrial Revenue Bonds with face value of $4,500,000 and $4,000,000. Monthly payments are for interest only on the bonds, and vary from month to month based on the interest rate during the period.

6The Tijuana plant has 2 temporary buildings measuring 45,000 sq. ft. and 40,000 sq. ft.

Item 3.

Legal Proceedings

The Company is involved in a dispute with Liberty Mutual, a former workers compensation administrator and stop-loss insurer for some of the Company s subsidiaries. The administrator has alleged that they are entitled to be reimbursed for certain costs incurred in administering various insurance claims. The Company has counter-sued,

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

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

From time to time, the Company is a party as plaintiff or defendant to various legal proceedings related to our normal business operations. In the opinion of management, although the outcome of any legal proceeding cannot be predicted with certainty, the ultimate liability of the Company in connection with its legal proceedings will not have a material adverse effect on the Company s financial position, but could be material to the results of operations in any one future accounting period. The Company makes appropriate reserves for litigation, even if not material. Defense costs are expensed as incurred.

Item 4.

Submission of Matters to a Vote of Security Holders

The Company held its annual meeting of shareholders on December 15, 2005. During the meeting, holders of 24,569,082 shares, representing ninety-three percent (93%) of the 26,310,551 shares outstanding on the record date, attended either in person or by proxy. Holders in excess of 90% of the totals vote cast voted for the election of members to the Board of Directors for Robert R. Amerson, Steven K. Clark, William Mitchum, Jr., Robert Kelly Barnhill, Sr., David M. Mock, and Peter Fredericks. As a result of the meeting, Messrs. Amerson, Clark, Mitchum, Barnhill, 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
2005		
Fourth Quarter ended December 31, 2005	$ 12.46	$ 9.81
Third Quarter ended September 30, 2005	$ 14.09	$ 8.85
Second Quarter ended June 30, 2005	$ 11.67	$ 7.77
First Quarter ended March 31, 2005	$ 11.43	$ 8.55
2004		
Fourth Quarter ended December 31, 2004	$ 10.17	$ 8.17
Third Quarter ended September 30, 2004	$ 10.47	$ 8.36
Second Quarter ended June 30, 2004	$ 9.99	$ 6.12
First Quarter ended March 31, 2004	$ 7.26	$ 5.21

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

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	1,535,000	$8.56	183,000
Long Term Incentive plan not approved by security holders			
Directors and Officers plan approved by security holders	257,000	$7.10	40,000
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 13, 2006, Flanders' common stock closed at $11.14. As of February 13, 2006, there were approximately 141 holders of record of the Company s common stock. The Company estimates there are approximately 3 beneficial owners (holders of more than 5% of the common stock) of the Company s common stock.

DIVIDENDS

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

SALES OF UNREGISTERED SECURITIES

The Company did not sell any unregistered securities during 2005, 2004 or 2003.

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.