

AAON INC
Form 10-Q
November 07, 2013

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

FORM 10-Q

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

For the quarterly period ended September 30, 2013
or

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

For the transition period from _____ to _____

Commission file number: 0-18953

AAON, INC.

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction

of incorporation or organization)

2425 South Yukon, Tulsa, Oklahoma 74107

(Address of principal executive offices)

(Zip Code)

87-0448736

(IRS Employer

Identification No.)

(918) 583-2266

(Registrant's telephone number, including area code)

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

Yes

No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes

No

Not Applicable

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

Large accelerated filer

Accelerated filer

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Non-accelerated filer

Smaller reporting company

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

Yes

No

As of November 5, 2013, registrant had outstanding a total of 36,748,489 shares of its \$.004 par value Common Stock.

AAON, Inc. and Subsidiaries
Consolidated Balance Sheets
(Unaudited)

| | September 30, 2013 | December 31, 2012 |
|--|---|----------------------|
| | (in thousands, except share and per share data) | |
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$2,289 | \$3,159 |
| Certificates of deposit | 8,186 | 3,120 |
| Investments held to maturity at amortized cost | 11,421 | 2,832 |
| Accounts receivable, net | 46,129 | 43,866 |
| Income tax receivable | 1,769 | 694 |
| Note receivable | 29 | 28 |
| Inventories, net | 33,383 | 32,614 |
| Prepaid expenses and other | 619 | 740 |
| Deferred tax assets | 5,296 | 4,493 |
| Total current assets | 109,121 | 91,546 |
| Property, plant and equipment: | | |
| Land | 1,353 | 1,340 |
| Buildings | 60,435 | 59,761 |
| Machinery and equipment | 122,356 | 117,617 |
| Furniture and fixtures | 9,539 | 8,906 |
| Total property, plant and equipment | 193,683 | 187,624 |
| Less: Accumulated depreciation | 105,975 | 96,929 |
| Property, plant and equipment, net | 87,708 | 90,695 |
| Certificates of deposit | 4,483 | 2,120 |
| Investments held to maturity at amortized cost | 17,867 | 8,041 |
| Note receivable | 959 | 1,091 |
| Total assets | \$220,138 | \$193,493 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Revolving credit facility | \$— | \$— |
| Accounts payable | 12,795 | 13,047 |
| Accrued liabilities | 30,314 | 26,578 |
| Total current liabilities | 43,109 | 39,625 |
| Deferred revenue | 358 | — |
| Deferred tax liabilities | 14,741 | 15,732 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Preferred stock, \$.001 par value, 5,000,000 shares authorized, no shares issued | — | — |
| Common stock, \$.004 par value, 168,750,000 shares authorized, 36,709,890 and 36,776,624 issued and outstanding at September 30, 2013 and December 31, 2012, respectively* | 147 | 147 |
| Additional paid-in capital | — | — |
| Retained earnings | 161,783 | 137,989 |
| Total stockholders' equity | 161,930 | 138,136 |

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| | | |
|--|-----------|-----------|
| Total liabilities and stockholders' equity | \$220,138 | \$193,493 |
|--|-----------|-----------|

*Reflects three-for-two stock split effective July 2, 2013

The accompanying notes are an integral part of these consolidated financial statements.

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

| | Three Months Ended | | Nine Months Ended | |
|--|---|------------|-------------------|------------|
| | September 30, | | September 30, | |
| | 2013 | 2012 | 2013 | 2012 |
| | (in thousands, except share and per share data) | | | |
| Net sales | \$89,690 | \$76,816 | \$247,764 | \$225,106 |
| Cost of sales | 63,074 | 59,667 | 178,160 | 173,336 |
| Gross profit | 26,616 | 17,149 | 69,604 | 51,770 |
| Selling, general and administrative expenses | 9,687 | 6,747 | 25,743 | 19,627 |
| Gain on disposal of assets | — | 4 | 52 | 17 |
| Income from operations | 16,929 | 10,406 | 43,913 | 32,160 |
| Interest expense | (1 |) (16 |) (2 |) (43 |
| Interest income | 61 | 40 | 153 | 55 |
| Other income (expense), net | 15 | 53 | 252 | 50 |
| Income before taxes | 17,004 | 10,483 | 44,316 | 32,222 |
| Income tax provision | 6,482 | 4,476 | 14,535 | 12,351 |
| Net income | \$10,522 | \$6,007 | \$29,781 | \$19,871 |
| Earnings per share: | | | | |
| Basic* | \$0.29 | \$0.16 | \$0.81 | \$0.54 |
| Diluted* | \$0.28 | \$0.16 | \$0.80 | \$0.54 |
| Cash dividends declared per common share*: | \$— | \$— | \$0.10 | \$0.08 |
| Weighted average shares outstanding: | | | | |
| Basic* | 36,742,262 | 36,803,235 | 36,752,657 | 36,837,686 |
| Diluted* | 37,017,561 | 37,001,127 | 37,041,775 | 37,083,695 |

*Reflects three-for-two stock split effective July 2, 2013

The accompanying notes are an integral part of these consolidated financial statements.

AAON, Inc. and Subsidiaries
 Consolidated Statements of Stockholders' Equity
 (Unaudited)

| | Common Stock | | Paid-in | Retained | |
|---|----------------|---------|-----------|------------|------------|
| | Shares* | Amount* | Capital | Earnings* | Total |
| | (in thousands) | | | | |
| Balances at December 31, 2012 | 36,777 | \$ 147 | \$— | \$ 137,989 | \$ 138,136 |
| Net income | — | — | — | 29,781 | 29,781 |
| Stock options exercised and restricted stock awards vested, including tax benefits | 171 | 1 | 1,487 | — | 1,488 |
| Share-based compensation | — | — | 1,054 | — | 1,054 |
| Stock repurchased and retired | (238) | (1) | (2,541) | (2,275) | (4,817) |
| Dividends** | — | — | — | (3,712) | (3,712) |
| Balances at September 30, 2013 | 36,710 | \$ 147 | \$— | \$ 161,783 | \$ 161,930 |

*Reflects three-for-two stock split effective July 2, 2013

**Includes cash payment of fractional shares from three-for-two stock split effective July 2, 2013

The accompanying notes are an integral part of these consolidated financial statements.

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

| | Nine Months Ended September 30, | |
|---|------------------------------------|----------|
| | 2013 | 2012 |
| | (in thousands) | |
| Operating Activities | | |
| Net income | \$29,781 | \$19,871 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 9,349 | 10,079 |
| Amortization of bond premiums | 545 | 80 |
| Provision for losses on accounts receivable, net of adjustments | 121 | (7) |
| Provision for excess and obsolete inventories | 468 | — |
| Share-based compensation | 1,054 | 625 |
| Excess tax benefits from stock options exercised and restricted stock awards vested | (502) | (267) |
| Gain on disposition of assets | (52) | (17) |
| Foreign currency transaction gain (loss) | 35 | (40) |
| Interest income on note receivable | (31) | — |
| Deferred income taxes | (1,794) | (987) |
| Write-off of note receivable | 75 | — |
| Changes in assets and liabilities: | | |
| Accounts receivable | (2,384) | (8,227) |
| Income tax receivable | 1,753 | 5,801 |
| Inventories | (1,237) | (2,702) |
| Prepaid expenses and other | 121 | 148 |
| Accounts payable | (227) | 2,681 |
| Deferred revenue | 358 | — |
| Accrued liabilities | 1,410 | 11,375 |
| Net cash provided by operating activities | 38,843 | 38,413 |
| Investing Activities | | |
| Capital expenditures | (6,407) | (12,582) |
| Proceeds from sale of property, plant and equipment | 72 | 311 |
| Investment in certificates of deposits | (8,869) | (4,280) |
| Maturities of certificates of deposits | 1,440 | 1,060 |
| Purchases of investments held to maturity | (22,275) | (5,624) |
| Maturities of investments | 3,315 | — |
| Proceeds from called investment | — | 270 |
| Principal payments from note receivable | 52 | 20 |
| Net cash used in investing activities | (32,672) | (20,825) |
| Financing Activities | | |
| Borrowings under revolving credit facility | 8,325 | 34,847 |
| Payments under revolving credit facility | (8,325) | (39,422) |
| Stock options exercised | 986 | 1,053 |
| Excess tax benefits from stock options exercised and restricted stock awards vested | 502 | 267 |
| Repurchase of stock | (4,817) | (4,379) |
| Cash dividends paid to stockholders | (3,712) | (2,950) |

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| | | | |
|--|---------|-----------|---|
| Net cash used in financing activities | (7,041 |) (10,584 |) |
| Net (decrease) increase in cash and cash equivalents | (870 |) 7,004 | |
| Cash and cash equivalents, beginning of period | 3,159 | 13 | |
| Cash and cash equivalents, end of period | \$2,289 | \$7,017 | |

The accompanying notes are an integral part of these consolidated financial statements.

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AAON, Inc., and Subsidiaries
Notes to the Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements of AAON, Inc., a Nevada corporation, and our operating subsidiaries, all of which are wholly-owned, (collectively, the “Company”) have been prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”) for interim financial information and with the rules and regulations of the Securities and Exchange Commission (“SEC”). These financial statements have not been audited by the Company's independent registered public accounting firm, except that the consolidated balance sheet at December 31, 2012 is derived from audited consolidated financial statements. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. The financial statements reflect all adjustments (all of which are of a normal recurring nature) which are, in the opinion of management, necessary for a fair statement of the results for the interim periods presented. Interim results are not necessarily indicative of the results that may be expected for a full year. Certain disclosures have been condensed in or omitted from these consolidated financial statements. The accompanying unaudited financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012. All intercompany balances and transactions have been eliminated in consolidation.

We are engaged in the manufacture and sale of air conditioning and heating equipment consisting of rooftop units, chillers, air-handling units, make-up air units, heat recovery units, condensing units and coils.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Because these estimates and assumptions require significant judgment, actual results could differ from those estimates and could have a significant impact on our results of operations, financial position and cash flows. We reevaluate our estimates and assumptions as needed, but at a minimum on a quarterly basis. The most significant estimates include, but are not limited to, the allowance for doubtful accounts, inventory reserves, warranty accrual, worker's compensation accrual, medical insurance accrual, income taxes and share-based compensation. Actual results could differ materially from those estimates.

Accounting Policies

A comprehensive discussion of our critical accounting policies and management estimates is included in Management’s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2012. There have been no significant changes in our critical accounting policies.

2. Revenue Recognition

We recognize revenues from sales of products when the title and risk of ownership pass to the customer. Final sales prices are fixed based on purchase orders. Sales allowances and customer incentives are treated as reductions to sales and are provided for based on historical experiences and current estimates. Sales of our products are moderately seasonal with the peak period being July - November of each year.

In addition, we present revenues net of sales tax and net of certain payments to our independent manufacturer representatives (“Representatives”). Representatives are national companies that are in the business of providing HVAC units and other related products and services to customers. The end user customer orders a bundled group of products and services from the Representative and expects the Representative to fulfill the order. Only after the specifications are agreed to by the Representative and the customer, and the decision is made to use an AAON HVAC unit, will we receive notice of the order. We establish the amount we must receive for our HVAC unit (“minimum sales price”), but do not control the total order price that is negotiated by the Representative with the end user customer.

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We are responsible for billings and collections resulting from all sales transactions, including those initiated by our Representatives. The Representatives submit the total order price to us for invoicing and collection. The total order price includes our minimum sales price and an additional amount which may include both the Representatives' fee and amounts due for additional products and services required by the customer. These additional products and services may include controls purchased from another manufacturer to operate the unit, start-up services, and curbs for supporting the unit ("Third Party Products"). All are associated with the purchase of a HVAC unit but may be provided by the Representative or another third party. The Company is under no obligation related to Third Party Products.

The Representatives' fee and Third Party Products amounts ("Due to Representatives") are paid only after all amounts associated with the order are collected from the customer. The amount of payments to our representatives were \$20.3 million and \$14.8 million for the three months ended September 30, 2013 and 2012, respectively. The amount of payments to our representatives were \$49.1 million and \$42.8 million for each of the nine months ended September 30, 2013 and 2012, respectively.

The Company also sells extended warranties on parts for various lengths of time ranging from 6 months to 10 years. Revenue for these separately priced warranties is deferred and recognized on a straight-line basis over the separately priced warranty period.

3. Investments

Certificates of Deposit – We held \$12.7 million and \$5.2 million in certificates of deposit at September 30, 2013, and December 31, 2012, respectively. At September 30, 2013, the certificates of deposit bear interest ranging from 0.10% to 0.90% per annum and have various maturities ranging from approximately two months to 18 months.

Investments Held to Maturity – Our investments held to maturity are comprised of \$29.3 million of corporate notes and bonds with original maturities ranging from less than one month to approximately 18 months. The investments have moderate risk with S&P ratings ranging from A+ to BBB-.

We record the amortized cost basis and accrued interest of the corporate notes and bonds in the Consolidated Balance Sheets. We record the interest and amortization of bond premium to interest income in the Consolidated Statements of Income.

The following summarizes the amortized cost and estimated fair value of our investments held to maturity as of September 30, 2013 and December 31, 2012:

| | Amortized Cost | Gross Unrealized Gain | Gross Unrealized (Loss) | Fair Value |
|------------------------------|-------------------|-----------------------------|-------------------------------|---------------|
| September 30, 2013: | (in thousands) | | | |
| Current assets: | | | | |
| Investments held to maturity | \$11,421 | \$3 | \$— | \$11,424 |
| Non current assets: | | | | |
| Investments held to maturity | 17,867 | — | (20 |) 17,847 |
| Total | \$29,288 | \$3 | \$(20 |) \$29,271 |
| December 31, 2012: | | | | |
| Current assets: | | | | |
| Investments held to maturity | \$2,832 | \$— | \$(1 |) \$2,831 |
| Non current assets: | | | | |
| Investments held to maturity | 8,041 | — | (9 |) 8,032 |

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| | | | | |
|-------|----------|-----|-------|------------|
| Total | \$10,873 | \$— | \$(10 |) \$10,863 |
|-------|----------|-----|-------|------------|

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4. Accounts Receivable

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

| | September 30, 2013 | December 31, 2012 |
|---------------------------------------|-----------------------|----------------------|
| | (in thousands) | |
| Accounts receivable | \$46,302 | \$43,918 |
| Less: Allowance for doubtful accounts | (173) | (52) |
| Total, net | \$46,129 | \$43,866 |

| | Three months ended | | Nine months ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 30, 2013 | September 30, 2012 | September 30, 2013 | September 30, 2012 |
| Allowance for doubtful accounts: | (in thousands) | | | |
| Balance, beginning of period | \$154 | \$242 | \$52 | \$268 |
| Provisions for losses on accounts receivables | 19 | (7) |) 121 | (8) |
| Accounts receivable written off, net of recoveries | — | (3) |) — | (28) |
| Balance, end of period | \$173 | \$232 | \$173 | \$232 |

5. Inventories

Inventories are valued at the lower of cost or market. Cost is determined by the first-in, first-out (“FIFO”) method. We establish an allowance for excess and obsolete inventories based on product line changes, the feasibility of substituting parts and the need for supply and replacement parts.

| | September 30, 2013 | December 31, 2012 |
|---|-----------------------|----------------------|
| | (in thousands) | |
| Raw materials | \$27,096 | \$28,155 |
| Work in process | 3,691 | 2,757 |
| Finished goods | 3,400 | 2,065 |
| | 34,187 | 32,977 |
| Less: Allowance for excess and obsolete inventories | (804) | (363) |
| Total, net | \$33,383 | \$32,614 |

The related changes in the allowance for excess and obsolete inventories account are as follows:

| | Three months ended | | Nine months ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 30, 2013 | September 30, 2012 | September 30, 2013 | September 30, 2012 |
| Allowance for excess and obsolete inventories: | (in thousands) | | | |
| Balance, beginning of period | \$537 | \$300 | \$363 | \$300 |
| Provisions for excess and obsolete inventories | 267 | — | 468 | — |
| Inventories written off | — | — | (27) |) — |
| Balance, end of period | \$804 | \$300 | \$804 | \$300 |

6. Supplemental Cash Flow Information

| | Three months ended | | Nine months ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 30, 2013 | September 30, 2012 | September 30, 2013 | September 30, 2012 |
| Supplemental disclosures: | (in thousands) | | | |
| Interest paid | \$ 1 | \$ 24 | \$ 1 | \$ 50 |
| Income taxes paid | 8,915 | 7,500 | 15,004 | 11,200 |
| Non-cash investing and financing activities: | | | | |
| Non-cash capital expenditures | (265 |) (1,723 |) 25 | (3,079 |
| Trade-in of equipment | — | — | — | 300 |

7. Warranties

The Company has warranties with various terms from eighteen months for parts to twenty-five years for certain heat exchangers. The Company has an obligation to replace parts or service its products if conditions under the warranty are met. A provision is made for estimated warranty costs at the time the related products are sold based upon the warranty period, historical trends, new products and any known identifiable warranty issues.

Changes in the warranty accrual are as follows:

| | Three months ended | | Nine months ended | |
|------------------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 30, 2013 | September 30, 2012 | September 30, 2013 | September 30, 2012 |
| Warranty accrual: | (in thousands) | | | |
| Balance, beginning of period | \$6,766 | \$6,575 | \$5,776 | \$6,093 |
| Payments made | (1,477 |) (1,036 |) (3,394 |) (3,128 |
| Provisions | 2,238 | 1,129 | 5,145 | 3,703 |
| Balance, end of period | \$7,527 | \$6,668 | \$7,527 | \$6,668 |
| Warranty expense: | \$2,289 | \$1,129 | \$5,332 | \$3,703 |

8. Accrued Liabilities

Accrued liabilities are as follows:

| | September 30, 2013 | December 31, 2012 |
|-----------------------------|-----------------------|----------------------|
| | (in thousands) | |
| Warranty | \$7,527 | \$5,776 |
| Due to representatives | 10,090 | 9,439 |
| Payroll | 3,676 | 3,852 |
| Worker's compensation | 678 | 928 |
| Medical self-insurance | 505 | 420 |
| Customer prepayments | 1,855 | 3,933 |
| Income tax payable | 2,326 | — |
| Employee benefits and other | 3,657 | 2,230 |
| Total | \$30,314 | \$26,578 |

9. Revolving Credit Facility

Our revolving credit facility provides for maximum borrowings of \$30.0 million which is provided by BOKF, NA dba Bank of Oklahoma, formerly known as Bank of Oklahoma, N.A. ("Bank of Oklahoma"). Under the line of credit, there is one standby letter of credit totaling \$0.9 million. Borrowings available under the revolving credit facility at September 30, 2013, were \$29.1 million. Interest on borrowings is payable monthly at LIBOR plus 2.5%. No fees are associated with the unused portion of the committed amount. We had no outstanding balance under the revolving credit facility at September 30, 2013 and December 31, 2012. Our weighted average interest rate was 2.69% at September 30, 2013 and 2.80% at December 31, 2012.

As of September 30, 2013, we were in compliance with our financial covenants. These covenants require that we meet certain parameters related to our tangible net worth, total liabilities to tangible net worth ratio and working capital. At September 30, 2013 our tangible net worth was \$161.9 million and met the requirement of being at or above \$95.0 million. Our total liabilities to tangible net worth ratio was 0.36 to 1, and met the requirement of not being above 2 to 1. Our working capital was \$66.0 million and met the requirement of being at or above \$40.0 million.

Effective July 28, 2013, the Company amended its revolving credit facility with the Bank of Oklahoma. The amendment extends the termination date of the revolving credit facility to July 27, 2014.

10. Income Taxes

Income tax expense for each of the three months ended September 30, 2013 and 2012, was \$6.5 million, or 38.1% of pre-tax income, and \$4.5 million, or 42.7% of pre-tax income, respectively. Income tax expense for each of the nine months ended September 30, 2013 and 2012, was \$14.5 million, or 32.8% of pre-tax income and \$12.4 million, or 38.3% of pre-tax income, respectively. The effective tax rate in 2012 was higher due to the loss of certain tax credits, as discussed below. Also, in the third quarter of 2012, the Company had some return to provision adjustments that caused the effective rate for that quarter to be higher than normal. The Company's estimated annual effective tax rate for the year 2013 is 33.4%. This differs from the U.S. federal statutory rate of 35% due to items such as state and local income taxes, Domestic Activities Deduction and various other federal and state income tax credits. Additionally, the income tax provision for the nine months ended September 30, 2013 reflects discrete benefits related to the Research and Development ("R&D") Credit and the Indian Employment Credit that were recorded in the first quarter of 2013. These federal credits were retroactively reinstated on January 2, 2013, with the enactment of the American Taxpayer Relief Act of 2012. No R&D Credit or Indian Employment Credit benefits were recorded in the income tax provision for 2012. The Company also had a change in estimate related to the recoverability of certain 2012 tax credits that was recorded in the first quarter of 2013, causing our effective tax rate to be lower than expected. This change in estimate was the result of additional and better information.

We file income tax returns in the U.S., state and foreign income tax returns jurisdictions. We are subject to U.S. examinations for tax years 2010 to present, and to non-U.S. income tax examinations for the tax years of 2007 through 2010. In addition, we are subject to state and local income tax examinations for the tax years 2009 to present. The Company continues to evaluate its need to file returns in various state jurisdictions and recorded \$0.2 million in additional state income tax expense, net of federal benefit, during the second quarter ended June 30, 2013, related to our updated assessment of required state filings. Any interest or penalties would be recognized as a component of income tax expense.

11. Share-Based Compensation

As discussed in Note 13, the Company had a three-for-two stock split effective July 2, 2013. All share information herein has been updated to reflect the effect of this stock split.

We have historically maintained a stock option plan for key employees, directors and consultants (“the 1992 Plan”). The 1992 Plan provided for 9.9 million shares to be issued under the plan in the form of stock options. Under the terms of the plan, the exercise price of shares granted may not be less than 85% of the fair market value at the date of the grant. Options granted to directors prior to May 25, 2004, vest one year from the date of grant and are exercisable for nine years thereafter. Options granted to directors on or after May 25, 2004, vest one-third each year, commencing one year after the date of grant. All other options granted vest at a rate of 20% per year, commencing one year after date of grant, and are exercisable during years 2-10.

On May 22, 2007, our stockholders adopted a Long-Term Incentive Plan (“LTIP”) which provides an additional 1,687,500 shares that can be granted in the form of stock options, stock appreciation rights, restricted stock awards, performance units and performance awards. Since inception of the plan, non-qualified stock options and restricted stock awards have been granted with the same vesting schedule as the previous plan. Under the LTIP, the exercise price of shares granted may not be less than 100% of the fair market value at the date of the grant.

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The total pre-tax compensation cost related to unvested stock options not yet recognized as of September 30, 2013 is \$2.0 million and is expected to be recognized over a weighted-average period of 2.3 years.

The following weighted average assumptions were used to determine the fair value of the stock options granted on the original grant date for expense recognition purposes for options granted during the nine months ended September 30, 2013 and 2012 using a Black Scholes Model:

| | Nine months ended | | | |
|--------------------------|-----------------------|-----------------------|--|---|
| | September 30, 2013 | September 30, 2012 | | |
| Director and Officers: | | | | |
| Expected dividend yield | 1.19 | % 1.23 | | % |
| Expected volatility | 47.08 | % 47.54 | | % |
| Risk-free interest rate | 1.55 | % 1.19 | | % |
| Expected life (in years) | 7 | 7 | | |
| Employees: | | | | |
| Expected dividend yield | 1.14 | % 1.23 | | % |
| Expected volatility | 45.92 | % 46.00 | | % |
| Risk-free interest rate | 1.40 | % 1.19 | | % |
| Expected life (in years) | 8 | 8 | | |

The expected term of the options is based on evaluations of historical and expected future employee exercise behavior. The risk-free interest rate is based on the U.S. Treasury rates at the date of grant with maturity dates approximately equal to the expected life at the grant date. Volatility is based on historical volatility of our stock over time periods equal to the expected life at grant date.

The following is a summary of stock options vested and exercisable as of September 30, 2013:

| Range of Exercise Prices | Number of Shares | Weighted Average Remaining Contractual Life (in years) | Weighted Average Exercise Price | Intrinsic Value (in thousands) |
|--------------------------|------------------|--|---------------------------------|--------------------------------|
| \$4.81-\$6.47 | 74,100 | 2.27 | \$5.50 | \$1,561 |
| \$6.80-\$8.65 | 209,850 | 4.58 | 7.18 | 4,067 |
| \$9.13-\$13.05 | 192,183 | 7.66 | 11.32 | 2,929 |
| Total | 476,133 | 5.46 | \$8.59 | \$8,557 |

The following is a summary of stock options vested and exercisable as of September 30, 2012:

| Range of Exercise Prices | Number of Shares | Weighted Average Remaining Contractual Life (in years) | Weighted Average Exercise Price | Intrinsic Value (in thousands) |
|--------------------------|------------------|--|---------------------------------|--------------------------------|
| \$4.81-\$6.47 | 140,025 | 2.90 | \$5.29 | \$1,072 |
| \$6.80-\$8.65 | 277,125 | 4.93 | 7.43 | 1,527 |

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| | | | | |
|-----------------|---------|------|--------|---------|
| \$9.13-\$11.17 | 73,650 | 8.14 | 10.28 | 196 |
| \$12.20-\$14.38 | 2,250 | 8.18 | 12.20 | 2 |
| Total | 493,050 | 4.85 | \$7.27 | \$2,797 |

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A summary of option activity under the plans is as follows:

| Options | Shares | Weighted Average Exercise Price |
|-----------------------------------|-----------|--|
| Outstanding at December 31, 2012 | 1,115,513 | \$10.15 |
| Granted | 47,500 | 17.70 |
| Exercised | (122,345 |) 7.93 |
| Forfeited or Expired | (40,575 |) 11.80 |
| Outstanding at September 30, 2013 | 1,000,093 | \$10.70 |
| Exercisable at September 30, 2013 | 476,133 | \$8.59 |

The total intrinsic value of options exercised during the nine months ended September 30, 2013 and 2012 was \$1.5 million and \$2.1 million, respectively. The cash received from options exercised during the nine months ended September 30, 2013 and 2012 was \$1.0 million and \$1.1 million, respectively. The impact of these cash receipts is included in financing activities in the accompanying Consolidated Statements of Cash Flows.

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

These awards are recorded at their fair value on the date of grant and compensation cost is recorded using straight-line vesting over the service period. At September 30, 2013, unrecognized compensation cost related to unvested restricted stock awards was approximately \$1.2 million, which is expected to be recognized over a weighted average period of 2.1 years.

A summary of the unvested restricted stock awards is as follows:

| Restricted stock | Shares | Weighted Average Grant Date Fair Value |
|--------------------------------|---------|---|
| Unvested at December 31, 2012 | 96,113 | \$12.11 |
| Granted | 36,304 | 19.29 |
| Vested | (35,138 |) 12.17 |
| Forfeited | (900 |) 8.50 |
| Unvested at September 30, 2013 | 96,379 | \$14.83 |

A summary of share-based compensation is as follows:

| | Three months ended | | Nine months ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 30, 2013 | September 30, 2012 | September 30, 2013 | September 30, 2012 |
| Grant date fair value of awards during the period: | (in thousands) | | | |
| Options | \$110 | \$104 | \$382 | \$2,541 |
| Restricted stock | 51 | 353 | 700 | 649 |
| Total | \$161 | \$457 | \$1,082 | \$3,190 |
| Share-based compensation expense: | | | | |
| Options | \$186 | \$175 | \$647 | \$384 |
| Restricted stock | 173 | 86 | 407 | 241 |
| Total | \$359 | \$261 | \$1,054 | \$625 |
| Income tax benefit related to share-based compensation: | | | | |
| Options | \$84 | \$229 | \$376 | \$247 |
| Restricted stock | 33 | 5 | 126 | 20 |
| Total | \$117 | \$234 | \$502 | \$267 |

12. Earnings Per Share

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

| | Three months ended | | Nine months ended | |
|--|---|-----------------------|-----------------------|-----------------------|
| | September 30, 2013 | September 30, 2012 | September 30, 2013 | September 30, 2012 |
| | (in thousands, except share and per share data) | | | |
| Numerator: | | | | |
| Net income | \$10,522 | \$6,007 | \$29,781 | \$19,871 |
| Denominator: | | | | |
| Basic weighted average shares* | 36,742,262 | 36,803,235 | 36,752,657 | 36,837,686 |
| Effect of dilutive stock options and restricted stock* | 275,299 | 197,892 | 289,118 | 246,009 |
| Diluted weighted average shares* | 37,017,561 | 37,001,127 | 37,041,775 | 37,083,695 |
| Earnings per share: | | | | |
| Basic* | \$0.29 | \$0.16 | \$0.81 | \$0.54 |
| Diluted* | \$0.28 | \$0.16 | \$0.80 | \$0.54 |
| Anti-dilutive shares: | | | | |
| Shares* | 24,900 | 746,363 | 177,513 | 746,363 |

*Reflects three-for-two stock split effective July 2, 2013

13. Stockholders' Equity

Stock Repurchase - On May 17, 2010, the Board authorized a stock buyback program, targeting repurchases of up to approximately 5% (approximately 1.95 million shares) of our outstanding stock from time to time in open market transactions. Since the inception of the program, we repurchased a total of approximately 1.1 million shares for an aggregate price of \$11.5 million, or an average price of \$10.69 per share. We purchased the shares at current market prices. No repurchases were made for the nine month period ended September 30, 2013 or 2012.

On July 1, 2005, we entered into a stock repurchase arrangement by which employee-participants in our 401(k) savings and investment plan are entitled to have shares of AAON stock in their accounts sold to us to provide diversification of their investments. The maximum number of shares to be repurchased is contingent upon the number of shares sold by employees. Through September 30, 2013, we repurchased approximately 3.0 million shares for an aggregate price of \$29.0 million, or an average price of \$9.67 per share. We purchased the shares at current market prices. For the nine months ended September 30, 2013 and 2012 we repurchased shares of approximately 0.21 million, respectively.

Periodically, the Board of Directors authorizes us to repurchase shares from certain directors and officers following their exercise of stock options. The maximum number of shares to be repurchased is contingent upon the number of shares sold. Through September 30, 2013, we repurchased approximately 1.1 million shares for an aggregate price of \$11.8 million, or an average price of \$10.47 per share. We purchased the shares at current market prices. For the nine months ended September 30, 2013 and 2012 we repurchased approximately 0.03 million and 0.13 million shares, respectively, under this program.

Dividends - At the discretion of the Board of Directors we pay semi-annual cash dividends. Board approval is required to determine the date of declaration and amount for each semi-annual dividend payment.

We declared dividends to shareholders of record at the close of business on June 11, 2012, which were paid on July 2, 2012. At a meeting of the Board of Directors on November 7, 2012, the Board declared a regular semi-annual cash dividend of \$0.08 per share, and, in view of our strong financial position, the Board also declared a one-time special cash dividend of \$0.08 per share. The dividends were paid to shareholders of record at the close of business on December 3, 2012 and paid on December 24, 2012, respectively.

On May 21, 2013, the Board of Directors declared a three-for-two stock split of the Company's common stock to be paid in the form of a stock dividend on July 2, 2013. Stockholders of record at the close of business on June 13, 2013 received one

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additional share for every two shares they held as of that date. All share and per share information has been updated to reflect the effects of this stock split.

On May 21, 2013, the Board of Directors approved a semi-annual cash dividend of \$0.10 per share, post split, to the holders of our outstanding Common Stock as of the close of business on June 13, 2013, the record date. Those dividends were paid on July 2, 2013.

At a meeting of the Board of Directors on November 6, 2013, the Board declared a regular semi-annual cash dividend of \$0.10 per share. The dividends are payable to shareholders of record at the close of business on December 2, 2013, the record date, and will be paid on December 23, 2013.

14. Commitments and Contingencies

We are subject to claims and legal actions that arise in the ordinary course of business. Management believes that the ultimate liability from these claims and actions, if any, will not have a material effect on our results of operations, financial position or cash flows.

We sometimes are party to short-term, cancelable and non-cancelable, fixed and variable price contracts with major suppliers for the purchase of raw material and component parts. We expect to receive delivery of raw materials for use in our manufacturing operations. These contracts are not accounted for as derivatives instruments because they meet the normal purchases and sales exemption.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and the notes thereto, which are included in this report, and our audited consolidated financial statements and the notes thereto, which are included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012. This discussion contains or incorporates by reference “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are not historical facts, but rather are based on expectations, estimates, assumptions and projections about our industry, business and future financial results, based on information available at the time this report is filed with the Securities and Exchange Commission or, with respect to any document incorporated by reference, available at the time that such document was prepared. Our actual results could differ materially from the results contemplated by these forward-looking statements due to a number of factors, including those identified in the section entitled “Forward-Looking Statements” in this Item 2 of this Quarterly Report on Form 10-Q and in the section entitled “Risk Factors” in Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 31, 2012. We do not assume any obligation to update or revise any forward-looking statements to reflect changed assumptions, the occurrence of anticipated or unanticipated events, new information or circumstances or otherwise, except as required by law.

Overview

We engineer, manufacture and market air-conditioning and heating equipment consisting of rooftop units, chillers, air-handling units, make-up air units, heat recovery units, condensing units, commercial self-contained units and coils. These products are marketed and sold to retail, manufacturing, educational, medical and other commercial industries. We market units to all 50 states in the United States and certain provinces in Canada. Foreign sales were approximately 6.7% of our total net sales for the nine months just ended and 6.0% of our sales during the same period of 2012.

Our business can be affected by a number of economic factors, including the level of economic activity in the markets in which we operate. The recent state of the economy has negatively impacted the commercial and industrial new construction markets. If there is a further decline in the economic activity in the U.S. or further deterioration in the capital markets it could affect the level of activity in the markets in which we operate and therefore could result in a decrease of our sales volume and profitability. Sales in the commercial and industrial new construction markets correlate closely to the number of new homes and buildings that are built, which in turn is influenced by cyclical factors such as interest rates, inflation, consumer spending habits, employment rates and other macroeconomic factors over which we have no control.

We sell our products to property owners and contractors through a network of manufacturers’ representatives and our internal sales force. Demand for our products is influenced by national and regional economic and demographic factors. The commercial and industrial new construction market is subject to cyclical fluctuations in that it is generally tied to housing starts, but has a lag factor of 6 to 18 months. Housing starts, in turn, are affected by such factors as interest rates, the state of the economy, population growth and the relative age of the population. When new construction is down, we emphasize the replacement market.

The principal components of cost of goods sold are labor, raw materials, component costs, factory overhead, freight out and engineering expense. The principal high volume raw materials used in our manufacturing processes are steel, copper and aluminum, which are obtained from domestic suppliers.

The price levels of our raw materials have somewhat moderated from the high prices we experienced a year ago, but the market continues to be volatile and unpredictable due to the economic environment and uncertainty in the financial

and capital markets. For the nine months ended September 30, 2013, the prices for copper, steel and aluminum decreased by approximately 2.27%, 5.83% and 5.15%, respectively, from the nine months ended September 30, 2012.

We attempt to limit the impact of price fluctuations on these materials by entering into cancelable and non-cancelable fixed price contracts with our major suppliers for periods of 6 to 18 months. We expect to receive delivery of raw materials from our fixed price contracts for use in our manufacturing operations. In addition, from time to time we use derivative contracts to partially mitigate the volatility in the prices for some of these commodities. We did not enter into a derivative contract for any of our key raw materials during the periods ended September 30, 2013 and 2012.

Key financial highlights impacting our financial condition, results of operations and cash position for the three months ended September 30, 2013 are as follows:

Net sales for the third quarter of 2013 increased by 16.8% to \$89.7 million compared to \$76.8 million for the same period in 2012.

Income from operations increased by \$6.5 million, or 62.7% to \$16.9 million from the same quarter a year ago.

We ended the quarter with a cash balance of \$2.3 million and no debt on our balance sheet. Working capital was \$66.0 million – an improvement of \$14.1 million, or 27.1% from the fourth quarter of 2012.

Cash provided by operations was \$38.8 million compared to \$38.4 million in the third quarter of 2012. Cash used in investing activities was \$32.7 million, which is \$11.8 million lower than the same period in 2012 primarily as a result of lower capital expenditures.

Net income was up by 75.2% or \$4.5 million to \$10.5 million in the third quarter of 2013 compared with net income of \$6.0 million for the same quarter in 2012. Basic and diluted earnings per share were \$0.29 and \$0.28, respectively, in the third quarter of 2013 compared to \$0.16 for both in the same period of 2012.

Results of Operations

Three Months Ended September 30, 2013 vs. Three Months Ended September 30, 2012

The following table provides a summary of our financial results, including information presented as a percentage of net sales (dollars in thousands):

| | Three months ended September 30, | | | | Percent of sales | | | |
|--|----------------------------------|----------|---------------------|----------|------------------|---------|---|---|
| | 2013 | 2012 | Increase (Decrease) | | 2013 | 2012 | | |
| | | | \$ | % | % | | % | % |
| Net sales | \$89,690 | \$76,816 | \$12,874 | 16.8 | % 100.0 | % 100.0 | | % |
| Cost of sales | 63,074 | 59,667 | 3,407 | 5.7 | % 70.3 | % 77.7 | | % |
| Gross profit | 26,616 | 17,149 | 9,467 | 55.2 | % 29.7 | % 22.3 | | % |
| Selling, general and administrative expenses | 9,687 | 6,747 | 2,940 | 43.6 | % 10.8 | % 8.8 | | % |
| (Gain) loss on disposal of assets | — | 4 | (4 |) (100.0 |)% — | — | | % |
| Income from operations | 16,929 | 10,406 | 6,523 | 62.7 | % 18.9 | % 13.5 | | % |
| Interest expense | (1 |) (16 |) 15 | (93.8 |)% — | — | | % |
| Interest income | 61 | 40 | 21 | 52.5 | % 0.1 | % 0.1 | | % |
| Other income (expense), net | 15 | 53 | (38 |) (71.7 |)% — | 0.1 | | % |
| Income before taxes | 17,004 | 10,483 | 6,521 | 62.2 | % 19.0 | % 13.6 | | % |
| Income tax provision | 6,482 | 4,476 | 2,006 | 44.8 | % 7.2 | % 5.8 | | % |
| Net income | \$10,522 | \$6,007 | \$4,515 | 75.2 | % 11.7 | % 7.8 | | % |

Net Sales

Net sales for the three months ended September 30, 2013 increased \$12.9 million, or 16.8%, to \$89.7 million from \$76.8 million over the same period in 2012. The increase in net sales is primarily attributed to gains in market share in the new commercial and industrial construction, and replacement markets and the result of product price increases introduced in April 2013.

Gross Profit

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For the quarter just ended September 30, 2013, gross profit increased \$9.5 million, or 55.2% to \$26.6 million from \$17.1 million for the same period a year ago. Gross profit as a percentage of net sales increased to 29.7% compared to 22.3% for the third quarter of 2012, primarily due to decreases in our raw material costs and the price increases from April 2013.

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Selling, General and Administrative Expenses

Selling, General and Administrative (“SG&A”) expenses increased by \$2.9 million, or 43.6% to \$9.7 million for the quarter just ended compared to \$6.7 million incurred in the third quarter of 2012. As a percentage of net sales, SG&A increased to 10.8% of total sales for the three months ended September 30, 2013 compared to 8.8% for the same period in 2012. Warranty expense increased \$1.2 million primarily due to the increases in sales. Profit sharing expense for the quarter increased \$0.9 million due to more favorable results in 2013 compared to 2012. Other primary increases in SG&A expense for the quarter include share-based compensation and other employee benefits.

Other Income (Expense)

Other income was \$0.02 million in the third quarter of 2013 compared to other income of \$0.1 million in the third quarter of 2012.

Income Taxes

Our effective rate for the three months ended September, 30, 2013 was 38.1% compared to 42.7% in the same period of 2012. Our effective tax rate differs from the statutory federal rate of 35% for certain items, such as state and local taxes, Domestic Activities Deduction, and other state and federal income tax credits. The Company had a return to provision adjustment in 2012 that caused the rate that quarter to be higher than expected.

Nine Months Ended September 30, 2013 vs. Nine Months Ended September 30, 2012

The following table provides a summary of our financial results, including information presented as a percentage of net sales (dollars in thousands):

| | Nine months ended September 30, | | | | Percent of sales | | | |
|--|---------------------------------|-----------|---------------------|-------|------------------|---------|---|--|
| | 2013 | 2012 | Increase (Decrease) | | 2013 | 2012 | | |
| | | | \$ | % | | | % | |
| Net sales | \$247,764 | \$225,106 | \$22,658 | 10.1 | % 100.0 | % 100.0 | % | |
| Cost of sales | 178,160 | 173,336 | 4,824 | 2.8 | % 71.9 | % 77.0 | % | |
| Gross profit | 69,604 | 51,770 | 17,834 | 34.4 | % 28.1 | % 23.0 | % | |
| Selling, general and administrative expenses | 25,743 | 19,627 | 6,116 | 31.2 | % 10.4 | % 8.7 | % | |
| Gain on disposal of assets | 52 | 17 | 35 | 205.9 | % — | — | | |
| Income from operations | 43,913 | 32,160 | 11,753 | 36.5 | % 17.7 | % 14.3 | % | |
| Interest expense | (2 |) (43 |) 41 | (95.3 |)% | — | — | |
| Interest income | 153 | 55 | 98 | 178.2 | % 0.1 | % — | | |
| Other income (expense), net | 252 | 50 | 202 | 404.0 | % 0.1 | % — | | |
| Income before taxes | 44,316 | 32,222 | 12,094 | 37.5 | % 17.9 | % 14.3 | % | |
| Income tax provision | 14,535 | 12,351 | 2,184 | 17.7 | % 5.9 | % 5.5 | % | |
| Net income | \$29,781 | \$19,871 | \$9,910 | 49.9 | % 12.0 | % 8.8 | % | |

Net Sales

Net sales for the nine months ended September 30, 2013 increased \$22.7 million, or 10.1%, to \$247.8 million from \$225.1 million over the same period in 2012. The overall increase in net sales is the result of warm winter weather that pulled forward construction and manufacturing spending activity early in the first half of 2013. In addition, the

increase is driven by gain in market share from new construction and replacement markets and product price increases introduced in April 2013.

Gross Profit

For the nine months ended September 30, 2013, gross profit increased \$17.8 million, or 34.4% to \$69.6 million from \$51.8 million for the same period a year ago. Gross profit as a percentage of net sales increased to 28.1% compared to 23.0% for the nine months ended September 30, 2012, primarily due to decreases in our raw material costs and the price increases in April 2013.

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Selling, General and Administrative Expenses

Selling, General and Administrative (“SG&A”) expenses increased by \$6.1 million, or 31.2% to \$25.7 million for the nine months just ended compared to \$19.6 million incurred in the same period of 2012. As a percentage of net sales, SG&A increased to 10.4% of total sales for the nine months ended September 30, 2013, compared to 8.7% for the same period in 2012. Warranty expense increased \$1.6 million due to increases in the Company's sales in recent periods. Profit sharing expense increased \$1.5 million due to more favorable results in 2013 compared to 2012. Other significant increases include stock-based compensation, employee benefits, professional fees from our auditors and external consultants, advertising and sales tax.

Other Income (Expense)

Other income was \$0.3 million in the nine months ended September, 30, 2013 compared to other income of \$0.1 million in the same period of 2012. In the second quarter 2013, the Company completed work done to repair its facilities from an ice storm in a prior year. The insurance proceeds received for this damage exceeded the cost to repair the buildings resulting in a gain of approximately \$0.3 million.

Income Taxes

Our effective rate for the nine months ended September, 30, 2013 was 32.8% compared to 38.3% in the same period of 2012. The income tax provision for the nine months ended September 30, 2013 reflected discrete benefits related to the Research and Development (“R&D”) Credit and the Indian Employment Credit. These federal credits were retroactively reinstated on January 2, 2013, with the enactment of the American Taxpayer Relief Act of 2012. No R&D Credit or Indian Employment Credit benefits were recorded in the income tax provision for the nine months ended September 30, 2012. The Company also had a change in estimate related to the recoverability of certain 2012 tax credits that was recorded in the first quarter of 2013, causing our effective tax rate to be lower than expected. This change in estimate was the result of additional and better information.

Liquidity and Capital Resources

Our primary sources of liquidity are cash flows generated from our operating activities and the borrowing capacity under the revolving line of credit provided by the Bank of Oklahoma, National Association. Our primary uses of cash are working capital, capital expenditures, contractual obligations, stock repurchases, and dividend payments.

General

Our revolving credit facility provides for maximum borrowings of \$30.0 million. We have a standby letter of credit that expires on December 31, 2013 of approximately \$0.9 million, which meets the requirement for our worker's compensation insurance program. There are no fees associated with the unused portion of the committed amount.

During the nine months ended September 30, 2013, we borrowed \$8.3 million and made payments of \$8.3 million under the revolving credit facility. Interest on borrowings is payable monthly at LIBOR plus 2.5%. We paid interest at a weighted average rate of 2.69% during the nine months just ended, and 2.80% for the year ended December 31, 2012.

We had no outstanding balance under the revolving credit facility at September 30, 2013 and December 31, 2012. Borrowings available under the revolving credit facility at September 30, 2013 were \$29.1 million.

As of September 30, 2013, we were in compliance with the financial covenants in the revolving credit facility and anticipate our compliance will continue during the remainder of 2013. These covenants require us to meet certain parameters related to our tangible net worth, total liabilities to tangible net worth ratio and working capital. At September 30, 2013, our tangible net worth was \$161.9 million, which meets the requirement of being at or above \$95.0 million. Our total liabilities to tangible net worth ratio was 0.36 to 1, which meets the requirement of not being above 2 to 1. Our working capital was \$66.0 million which meets the requirement of being at or above \$40.0 million.

For the nine months just ended in 2013, we repurchased shares of stock under our authorized stock buyback programs, employees' 401(k) savings, investment plan, and from options exercised by our directors and officers in the open market in the amount of \$4.8 million for approximately 0.24 million shares, as compared to \$4.4 million for approximately 0.34 million shares for the same period in 2012.

Management believes that our projected cash flows from operations and the revolving credit facility, or comparable financing, will provide the necessary liquidity and capital resources for fiscal year 2013 and the foreseeable future. This expectation is based upon, among other things, our knowledge of the heating, ventilation, and air conditioning (“HVAC”) industry, our leadership in the industry, our sales volumes, market prices for our products, our ability to limit the growth of our business if necessary, our ability to adjust dividend cash payments, our relationship with the existing bank lender, in addition to general industry and economic conditions.

Statement of Cash Flows

The following table reflects the major categories of cash flows for the nine months ended September 30, 2013 and 2012. For additional details, see the Condensed Consolidated Statements of Cash Flows in the condensed consolidated financial statements.

| | 2013 | 2012 |
|---|----------------|----------|
| | (in thousands) | |
| Net cash provided by operating activities | \$38,843 | \$38,413 |
| Net cash used in investing activities | (32,672) | (20,825) |
| Net cash used in financing activities | (7,041) | (10,584) |

Cash Flows Provided by Operating Activities

For the nine months just ended in 2013, cash provided by operations amounted to \$38.8 million as compared to \$38.4 million in the same period of 2012. The increase in cash flows is due to an increase in net income of \$9.9 million offset by a decrease in changes in working capital of \$9.3 million. Significant fluctuations in working capital were as follows:

Increased accounts receivable was a use of cash of \$2.4 million during the nine months just ended in 2013 primarily as a result of increased sales.

Income tax receivable increased cash by \$1.8 million during the nine months ended September 30, 2013, as the Company had overpayments which can be applied in the current period.

Payables and accrued expenses increased cash by \$1.2 million mainly as a result of increased amounts due to our representatives, payroll and employee benefits.

Cash Flows Used in Investing Activities

Cash used in investing activities was \$32.7 million in the nine months just ended in 2013 as compared to \$20.8 million for the same period of 2012. The 2013 use of cash in investing activities is primarily related to purchases of CDs and investments of \$31.1 million, partially offset by proceeds from the maturity of CDs and investments of approximately \$4.8 million. Additionally, the Company has decreased capital expenditures of \$6.2 million in 2013 compared with 2012.

Cash Flows Used in Financing Activities

Cash used in financing activities was \$7.0 million in the nine months just ended in 2013 as compared to \$10.6 million for the same period of 2012. The most significant item affecting the comparison of our financing cash flows for these periods relates to net payments of zero on our line of credit in the nine months ended September 30, 2013 compared to \$4.6 million in the same period in 2012.

Off-Balance Sheet Arrangements

We are not party to any off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenues, expenses, results of operations, liquidity, capital expenditures or capital resources.

Contractual Obligations

As of September 30, 2013, there have been no material changes outside the ordinary course of business in the contractual obligations disclosed in our Annual Report on Form 10-K for the year ended December 31, 2012 under the caption "Contractual Obligations."

Critical Accounting Policies

There have been no material changes in the Company's critical accounting policies during the nine months ended September 30, 2013.

Forward-Looking Statements

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Interest Rate Risk

We are subject to interest rate risk on the revolving credit facility which bears variable interest based upon a rate of LIBOR plus 2.5%. At September 30, 2013, the available balance under the revolving credit facility was \$29.1 million.

Commodity Price Risk

Our exposure to commodity cost risk is related primarily to the price of copper, steel, and aluminum, as these are major components of our product cost. We are exposed to volatility in the prices of these commodities and occasionally we use fixed price cancellable and non-cancellable contracts with our major suppliers for periods of 6 to 18 months to manage this exposure.

Item 4. Controls and Procedures.

(a) Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this Quarterly Report on Form 10-Q (the Evaluation Date), we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer with the oversight of the Audit Committee, regarding the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded, as of the end of the period covered by this Quarterly Report, that our disclosure controls and procedures were effective.

(b) Previously Reported Material Weaknesses in Internal Control over Financial Reporting

As reported in our assessment of the effectiveness of our internal control over financial reporting as of December 31, 2012, included in “Item 9A. Controls and Procedures” of Form 10-K for the year ended December 31, 2012, a material weakness existed in the review procedures associated with key financial statement elements related to inter-company activities, income taxes and inventory.

Remediation Efforts in 2013

To remediate the material weakness described above and improve the operational effectiveness of our internal control over financial reporting, management made the following changes in the first quarter of 2013:

- The Company hired a new Chief Accounting Officer with requisite technical and financial reporting skills to help address the identified matters.

- Management created a better model for analyzing inventory variances.

- Management improved the verification process relating to accuracy of reports and data used in critical calculations.

- Management designed a process and controls to ensure a more precise review is performed for manual journal entries relating to critical calculations and estimates.

The Company plans to continue to improve its processes and controls through training and education, automation and strengthening of controls procedures in areas which involve significant judgments and estimates.

Management believes that these measures will mitigate the material weakness described above. The Audit Committee and the Board of Directors and management monitor the effectiveness of our internal controls and procedures on an ongoing basis. The material weakness is fully remediated when, in the opinion of management, the revised control processes have been operating for a sufficient period of time to provide reasonable assurance as to their effectiveness. The Company anticipates that it will complete its testing of the additional internal control processes during the balance of 2013. We will continue to assess the effectiveness of our remediation efforts in connection with management's future evaluations of internal control over financial reporting.

(c) Changes in Internal Control over Financial Reporting

There have been no changes in internal control over financial reporting that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II – OTHER INFORMATION

Item 1A. Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2012. The risk factors described in our Annual Report could materially adversely affect our business, financial condition or future results. There have been no other material changes to the risk factors included in our 2012 Annual Report.

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

On May 17, 2010, the Board authorized a stock buyback program, targeting repurchases of up to approximately 5% (1.95 million shares) of our outstanding stock from time to time in open market transactions. Since the inception of the program, we repurchased a total of approximately 1.1 million shares under this program for an aggregate price of \$11.5 million, or an average price of \$10.69 per share. We purchased the shares at current market prices. No purchases were made for the nine month period ended September 30, 2013 or 2012.

On July 1, 2005, we entered into a stock repurchase arrangement by which employee-participants in our 401(k) savings and investment plan are entitled to have shares of AAON stock in their accounts sold to us to provide diversification of their investments. The maximum number of shares to be repurchased is contingent upon the number of shares sold by employees. Through September 30, 2013, we repurchased approximately 3.0 million shares for an aggregate price of \$29.0 million, or an average price of \$9.67 per share. We purchased the shares at current market prices.

Periodically, the Board of Directors authorizes us to repurchase shares from certain directors and officers following their exercise of stock options. The maximum number of shares to be repurchased is contingent upon the number of shares sold. Through September 30, 2013, we repurchased approximately 1.1 million shares for an aggregate price of \$11.8 million, or an average price of \$10.47 per share. We purchased the shares at current market prices.

Repurchases during the third quarter of 2013 were as follows:

ISSUER PURCHASES OF EQUITY SECURITIES

| Period | (a) Total Number of Shares (or Units) Purchased | (b) Average Price Paid Per Share (or Unit) | (c) Total Number of Shares (or Units) Purchased as part of Publicly Announced Plans or Programs | (d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that may yet be Purchased under the Plans or Programs |
|----------------|--|---|---|--|
| July 2013 | 19,725 | \$23.61 | 19,725 | — |
| August 2013 | 22,342 | 24.00 | 22,342 | — |
| September 2013 | 31,883 | 25.09 | 31,883 | — |
| Total | 73,950 | \$24.37 | 73,950 | — |

Item 4. Mine Safety Disclosures

Not applicable

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

None.

Item 5. Other Information.

None.

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Item 6. Exhibits.

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

SIGNATURES

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

AAON, INC.

Dated: November 7, 2013

By: /s/ Norman H. Asbjornson
Norman H. Asbjornson
President/CEO

Dated: November 7, 2013

By: /s/ Scott M. Asbjornson
Scott M. Asbjornson
Chief Financial Officer