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, 2021

or

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

For the transition period from ____________________ to ____________________

Commission file number: 0-18953

AAON, INC.

(Exact name of registrant as specified in its charter)

Nevada	87-0448736
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

2425 South Yukon Ave., Tulsa, Oklahoma 74107
(Address of principal executive offices) (Zip Code)

(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 every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☑ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definition of "large accelerated filer", "accelerated filer", "small reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☑	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

Yes ☐ No ☑

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	AAON	NASDAQ

As of November 1, 2021, registrant had outstanding a total of 52,428,030 shares of its $.004 par value Common Stock.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

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

	September 30, 2021	December 31, 2020
Assets	*(in thousands, except share and per share data)*	
Current assets:		
Cash and cash equivalents	$ 101,813	$ 79,025
Restricted cash	660	3,263
Accounts receivable, net of allowance for credit losses of $477 and $506, respectively	58,756	47,387
Income tax receivable	1,999	4,587
Note receivable	32	31
Inventories, net	104,553	82,219
Prepaid expenses and other	2,802	3,739
Total current assets	270,615	220,251
Property, plant and equipment:		
Land	5,016	4,072
Buildings	131,327	122,171
Machinery and equipment	299,226	281,266
Furniture and fixtures	21,679	18,956
Total property, plant and equipment	457,248	426,465
Less: Accumulated depreciation	216,667	203,125
Property, plant and equipment, net	240,581	223,340
Goodwill and intangible assets, net	3,229	3,267
Right of use assets	1,421	1,571
Note receivable	557	579
Total assets	$ 516,403	$ 449,008
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$ 25,940	$ 12,447
Accrued liabilities	48,266	46,586
Total current liabilities	74,206	59,033
Deferred tax liabilities	31,090	28,324
Other long-term liabilities	4,434	4,423
New market tax credit obligation (a)	6,394	6,363
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $.001 par value, 5,000,000 shares authorized, no shares issued	—	—
Common stock, $.004 par value, 100,000,000 shares authorized, 52,420,486 and 52,224,767 issued and outstanding at September 30, 2021 and December 31, 2020, respectively	210	209
Additional paid-in capital	11,966	5,161
Retained earnings	388,103	345,495
Total stockholders' equity	400,279	350,865
Total liabilities and stockholders' equity	$ 516,403	$ 449,008

(a) Held by variable interest entities (Note 14)

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

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

	Three Months Ended September 30, 2021	Three Months Ended September 30, 2020	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020
	(in thousands, except share and per share data)			
Net sales	$ 138,571	$ 134,772	$ 398,235	$ 397,851
Cost of sales	102,552	93,924	286,952	275,925
Gross profit	36,019	40,848	111,283	121,926
Selling, general and administrative expenses	15,897	14,716	47,488	45,869
Gain on disposal of assets	(15)	1	(15)	(61)
Income from operations	20,137	26,131	63,810	76,118
Interest (expense) income, net	(10)	10	(11)	90
Other (expense) income, net	(19)	15	37	20
Income before taxes	20,108	26,156	63,836	76,228
Income tax provision	4,527	5,696	11,264	16,111
Net income	$ 15,581	$ 20,460	$ 52,572	$ 60,117
Earnings per share:				
Basic	$ 0.30	$ 0.39	$ 1.00	$ 1.15
Diluted	$ 0.29	$ 0.38	$ 0.98	$ 1.14
Cash dividends declared per common share:	$ —	$ —	$ 0.19	$ 0.19
Weighted average shares outstanding:				
Basic	52,420,711	52,260,551	52,392,300	52,174,705
Diluted	53,546,513	53,151,295	53,664,997	52,955,049

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

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

	Nine Months Ended September 30, 2021				
	Common Stock		Paid-in	Retained	
	Shares	Amount	Capital	Earnings	Total
			(in thousands)		
Balances at December 31, 2020	52,225	$ 209	$ 5,161	$ 345,495	$ 350,865
Net income	—	—	—	52,572	52,572
Stock options exercised and restricted stock awards granted	438	2	14,571	—	14,573
Share-based compensation	—	—	8,784	—	8,784
Stock repurchased and retired	(243)	(1)	(16,550)	—	(16,551)
Dividends	—	—	—	(9,964)	(9,964)
Balances at September 30, 2021	52,420	$ 210	$ 11,966	$ 388,103	$ 400,279

	Three Months Ended September 30, 2021				
	Common Stock		Paid-in	Retained	
	Shares	Amount	Capital	Earnings	Total
			(in thousands)		
Balances at June 30, 2021	52,416	$ 210	$ 10,998	$ 372,518	$ 383,726
Net income	—	—	—	15,581	15,581
Stock options exercised and restricted stock awards granted	77	—	2,725	—	2,725
Share-based compensation	—	—	2,991	—	2,991
Stock repurchased and retired	(73)	—	(4,748)	—	(4,748)
Dividends	—	—	—	4	4
Balances at September 30, 2021	52,420	$ 210	$ 11,966	$ 388,103	$ 400,279

	Nine Months Ended September 30, 2020				
	Common Stock		Paid-in	Retained	
	Shares	Amount	Capital	Earnings	Total
			(in thousands)		
Balances at December 31, 2019	52,079	$ 208	$ 3,631	$ 286,301	290,140
Net income	—	—	—	60,117	60,117
Stock options exercised and restricted stock awards granted	616	2	18,517	—	18,519
Share-based compensation	—	—	8,546	—	8,546
Stock repurchased and retired	(430)	(1)	(22,519)	—	(22,520)
Dividends	—	—	—	(9,910)	(9,910)
Balances at September 30, 2020	52,265	$ 209	$ 8,175	$ 336,508	$ 344,892

	Three Months Ended September 30, 2020				
	Common Stock		Paid-in	Retained	
	Shares	Amount	Capital	Earnings	Total
			(in thousands)		
Balances at June 30, 2020	52,234	$ 209	$ 6,451	$ 316,035	$ 322,695
Net income	—	—	—	20,460	20,460
Stock options exercised and restricted stock awards granted	126	—	4,346	—	4,346
Share-based compensation	—	—	2,852	—	2,852
Stock repurchased and retired	(95)	—	(5,474)	—	(5,474)
Dividends	—	—	—	13	13
Balances at September 30, 2020	52,265	$ 209	$ 8,175	$ 336,508	$ 344,892

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,	
	2021	**2020**
Operating Activities	*(in thousands)*	
Net income	$ 52,572	$ 60,117
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	22,532	18,971
Amortization of debt issuance cost	31	31
Provision for credit losses on accounts receivable, net of adjustments	—	193
Provision for excess and obsolete inventories	378	1,776
Share-based compensation	8,784	8,546
(Gain) loss on disposition of assets	(15)	(61)
Foreign currency transaction (gain) loss	(1)	18
Interest income on note receivable	(19)	(19)
Deferred income taxes	2,766	7,676
Changes in assets and liabilities:		
Accounts receivable	(11,369)	5,011
Income taxes	2,588	(3,142)
Inventories	(22,712)	(6,994)
Prepaid expenses and other	937	(598)
Accounts payable	16,390	3,654
Deferred revenue	316	1,128
Accrued liabilities	1,525	688
Net cash provided by operating activities	74,703	96,995
Investing Activities		
Capital expenditures	(42,636)	(48,955)
Proceeds from sale of property, plant and equipment	19	61
Principal payments from note receivable	41	38
Net cash used in investing activities	(42,576)	(48,856)
Financing Activities		
Stock options exercised	14,573	18,519
Repurchase of stock	(15,014)	(21,390)
Employee taxes paid by withholding shares	(1,537)	(1,130)
Cash dividends paid to stockholders	(9,964)	(9,910)
Net cash used in financing activities	(11,942)	(13,911)
Net increase in cash, cash equivalents and restricted cash	20,185	34,228
Cash, cash equivalents and restricted cash, beginning of period	82,288	44,373
Cash, cash equivalents and restricted cash, end of period	$ 102,473	$ 78,601

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

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

1. General

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”).

Our financial statements consolidate all of our affiliated entities in which we have a controlling financial interest. Because we hold certain rights that give us the power to direct the activities of two variable interest entities ("VIEs") (Note 14) that most significantly impact the VIEs economic performance, combined with a variable interest that gives us the right to receive potentially significant benefits or the obligation to absorb potentially significant losses, we have a controlling financial interest in those VIEs.

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, 2020 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, 2020. All intercompany balances and transactions have been eliminated in consolidation.

We are engaged in the engineering, manufacturing, marketing, and sale of air conditioning and heating equipment consisting of standard, semi-custom and custom rooftop units, chillers, packaged outdoor mechanical rooms, air handling units, makeup air units, energy recovery units, condensing units, geothermal/water-source heat pumps, coils, and controls.

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, 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.

Impact of February 2021 Weather

In February 2021, record-breaking winter storms affected Oklahoma and Texas, causing sustained below freezing temperatures, hazardous driving conditions, rolling blackouts, water main breaks, and a host of other weather related issues. In addition to significant absenteeism as a result of employees being unable to travel to and from work due to inadequate transportation and/or hazardous road conditions, the Company made the decision to shut down the Tulsa, OK and Longview, TX plants for several days. This decision was based on the expected employee absenteeism as well as the expected rolling blackouts caused by the increased demand on the electrical and natural gas power grids. Although we lost several production days in mid-February 2021, we do not believe that the impact of this weather event had a material adverse effect on the results of our operations, financial position and cash flows as of and for the year ending December 31, 2021.

Impact of COVID-19 Pandemic

In March 2020, the World Health Organization characterized the coronavirus ("COVID-19") a pandemic, and the President of the United States declared the COVID-19 outbreak a national emergency. The rapid spread of the pandemic and the continuously evolving responses to combat it have had an increasingly negative impact on the global economy.

Our manufacturing operations are considered a critical infrastructure industry, as defined by the U.S. Department of Homeland Security, as such, the decrees issued by national, state, and local governments in response to the COVID-19 pandemic have had minimal impact on our operations except for higher employee absenteeism, mostly in June 2020, in our manufacturing facilities. Our Longview, TX facility suffered from COVID-19 related absenteeism in the quarter ending September 30, 2021, which reduced the production of coils that were needed to complete units at our Tulsa, OK facility. We maintained continuous operations during the nine months ended September 30, 2021, except for planned maintenance in January and the weather related shutdown in February 2021. For the most part, our workers are able to socially distance themselves during the manufacturing process. Additional precautions have been taken to social distance workers that work in close environments and we have facilitated voluntary on-site COVID-19 vaccine clinics. The Company utilizes sanitation stations and performs additional cleaning and sanitation throughout the day.

We witnessed increases in some of our raw material prices, especially in copper and steel, which appear to be an impact of COVID-19, and have put in place price increases in our products and continue to make strategic purchases of materials when we see opportunities. Although, we have experienced some supply chain challenges, due to our strong vendor relationships as well as our favorable liquidity position, we have experienced minimal disruption to our supply chain due to COVID-19. We anticipate that the average cost of raw materials and certain components purchased, including the impact of rising inflation and tariffs, for the remainder of 2021 will be higher than the costs experienced during the year ended December 31, 2020.

The magnitude of the impact of COVID-19 remains unpredictable and we, therefore, continue to anticipate potential supply chain disruptions, some employee absenteeism, and additional health and safety costs related to the COVID-19 pandemic that could unfavorably impact our business. While our supply chain disruptions to date have been minimal and intermittent, they have impacted the production process which creates inefficiencies and can deteriorate our profit margins.

Additionally, we continue to experience challenges in a tight labor market, especially the hiring of both skilled and unskilled production labor. In July 2021, we increased starting wages for our production workforce by 7.0%. We also have put a cost of living increase of 3.5% in place in October for all employees below the Director level. We will continue to implement human resource initiatives to retain and attract labor to further improve productivity and production efficiencies.

Because we have managed to maintain almost continuous operations with reasonable lead times through 2020 and 2021, our order intake is strong and has increased throughout 2021 as the economy has opened back up and COVID-19 restrictions have lessened. We expect to increase our production for the remainder of 2021 and into 2022.

We do not believe that the impact of the COVID-19 pandemic will have a material adverse effect on the results of our operations, financial position and cash flows as of and for the year ended December 31, 2021. However, we are continually monitoring the progression of the COVID-19 pandemic, including the recent Delta variant, and its potential effects on our financial position, results of operations, and cash flows.

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, 2020.

Fair Value Measurements

We adopted ASU No. 2018-13, *Fair Value Measurements (Topic 820)*, as amended, as of January 1, 2020. The ASU includes additional disclosure requirements for unrealized gains and losses for Level 3 fair value measurements and significant observable inputs used to develop Level 3 fair value measurements. There was not a material impact to financial statements upon adoption. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date. Fair value is based upon assumptions that market participants would use when pricing an asset or liability. We use the following fair value hierarchy, which prioritizes valuation technique inputs used to measure fair value into three broad levels:

- Level 1: Quoted prices in active markets for identical assets and liabilities that we have the ability to access at the measurement date.
- Level 2: Inputs (other than quoted prices included within Level 1) that are either directly or indirectly observable for the asset or liability, including (i) quoted prices for similar assets or liabilities in active markets, (ii) quoted prices for identical or similar assets or liabilities in inactive markets, (iii) inputs other than quoted prices that are observable for the asset or liability, and (iv) inputs that are derived from observable market data by correlation or other means.
- Level 3: Unobservable inputs for the asset or liability including situations where there is little, if any, market activity for the asset or liability. Items categorized in Level 3 include the estimated fair values of property, plant and equipment, intangible assets, and goodwill acquired in a business combination.

The fair value hierarchy gives the highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable inputs (Level 3). In some cases, the inputs used to measure fair value might fall into different levels of the fair value hierarchy. The lowest level input that is significant to a fair value measurement determines the applicable level in the fair value hierarchy. Assessing the significance of a particular input to a fair value measurement requires judgment, considering factors specific to the asset or liability.

Intangible Assets

Our intangible assets include various trademarks, service marks and technical knowledge acquired in our February 2018 business combination. We amortize our intangible assets on a straight-line basis over the estimated useful lives of the assets. We evaluate the carrying value of our amortizable intangible assets for potential impairment when events and circumstances warrant such a review. As of March 31, 2021, our intangible assets were fully amortized. As of December 31, 2020, our intangible assets, net of amortization, were approximately $38 thousand. The amount of amortization was $58 thousand for the three months ended September 30, 2020 and $38 thousand and $175 thousand for the nine months ended September 30, 2021 and 2020, respectively.

Goodwill

Goodwill represents the excess of the consideration paid for the acquired business, in our February 2018 business combination, over the fair value of the individual assets acquired, net of liabilities assumed. Goodwill at September 30, 2021 is deductible for income tax purposes. Goodwill is not amortized, but instead is evaluated for impairment at least annually. We perform our annual assessment of impairment during the fourth quarter of our fiscal year, and more frequently if circumstances warrant. As of September 30, 2021 and December 31, 2020, our goodwill was approximately $3.2 million.

Recent Accounting Pronouncements

Changes to U.S. GAAP are established by the Financial Accounting Standards Board ("FASB") in the form of Accounting Standards Updates ("ASUs") to the FASB's Accounting Standards Codification ("ASC"). We consider the applicability and impact of all ASUs. ASUs were assessed and determined to be either not applicable or are expected to have minimal impact on our consolidated financial statements and notes thereto.

2. Revenue Recognition

Disaggregated net sales by major source:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(in thousands)			
Rooftop units	$ 103,900	$ 102,750	$ 298,695	$ 312,725
Condensing units	6,797	6,304	20,630	15,307
Air handlers	6,279	5,805	19,958	18,068
Outdoor mechanical rooms	208	867	1,183	2,216
Water source heat pumps	5,215	6,770	16,305	14,269
Part sales	12,102	10,484	30,325	24,562
Other	4,070	1,792	11,139	10,704
Net Sales	$ 138,571	$ 134,772	$ 398,235	$ 397,851

Disaggregated units sold by major source:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Rooftop units	3,746	4,372	11,362	12,179
Condensing units	560	593	1,696	1,447
Air handlers	646	534	1,846	1,545
Outdoor mechanical rooms	2	6	22	22
Water source heat pumps	1,576	1,847	5,108	5,109
Total Units	6,530	7,352	20,034	20,302

The Company recognizes revenue, presented net of sales tax, when it satisfies the performance obligation in its contracts. The primary performance obligation in our contract is delivery of the requested manufactured equipment. Most of the Company’s products are highly customized, cannot be resold to other customers and the cost of rework to be resold is not economical. The Company has a formal cancellation policy and generally does not accept returns on these units. As a result, many of the Company’s products do not have an alternative use and therefore, for these products we recognize revenue over the time it takes to produce the unit. For all other products that are part sales or standardized units, we satisfy the performance obligation when the control is passed to the customer, generally at time of shipment. 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 May-October of each year.

We are responsible for billings and collections resulting from all sales transactions, most of which are initiated by our independent manufacturer representatives (“Representatives”). Representatives are national companies that are in the business of providing heating, ventilation, and air conditioning ("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. These additional products and services may include, without limitation, controls purchased from another manufacturer to operate the unit, start-up services, and curbs for supporting the unit (“Third Party Products”). All of these items are associated with the purchase of a HVAC unit but may be provided by the Representative or another third party. 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. 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. The Company is considered the principal for the equipment we design and manufacture and records that revenue. The Company has no control over the Third Party Products to the end customer and the Company is under no obligation related to the Third Party Products. Amounts related to Third Party Products are not recognized as revenue but are recorded as a liability and are included in accrued liabilities on the consolidated balance sheet.

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 $9.5 million and $11.5 million for the three months ended September 30, 2021 and 2020, respectively. The amount of payments to our Representatives were $34.5 million and $39.0 million for the nine months ended September 30, 2021 and 2020, respectively.

The Company also sells extended warranties on parts for various lengths of time ranging from six 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. Accounts Receivable

Accounts receivable and the related allowance for credit losses are as follows:

	September 30, 2021	December 31, 2020
	(in thousands)	
Accounts receivable	$ 59,233	$ 47,893
Less: Allowance for credit losses	(477)	(506)
Total, net	$ 58,756	$ 47,387

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Allowance for credit losses:	*(in thousands)*			
Balance, beginning of period	$ 518	$ 429	$ 506	$ 353
Provisions (recoveries) for expected credit losses, net of adjustments	(12)	117	—	193
Accounts receivable written off, net of recoveries	(29)	—	(29)	—
Balance, end of period	$ 477	$ 546	$ 477	$ 546

4. Inventories

Inventories are valued at the lower of cost or net realizable value. 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.

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

	September 30, 2021	December 31, 2020
	(in thousands)	
Raw materials	$ 97,167	$ 76,238
Work in process	4,749	2,088
Finished goods	4,929	7,154
Total, gross	106,845	85,480
Less: Allowance for excess and obsolete inventories	(2,292)	(3,261)
Total, net	$ 104,553	$ 82,219

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Allowance for excess and obsolete inventories:	*(in thousands)*			
Balance, beginning of period	$ 2,726	$ 2,373	$ 3,261	$ 2,644
Provisions for excess and obsolete inventories	86	1,969	378	1,776
Inventories written off	(520)	(230)	(1,347)	(308)
Balance, end of period	$ 2,292	$ 4,112	$ 2,292	$ 4,112

5. Supplemental Cash Flow Information

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Supplemental disclosures:	*(in thousands)*			
Income taxes paid	$ 3,167	$ 1,841	$ 5,909	$ 11,576
Non-cash investing and financing activities:				
Non-cash capital expenditures[1]	$ (1,052)	$ (4,421)	$ (2,897)	$ 625

[1] Includes non-cash changes in accrued capital expenditures

6. Warranties

The Company has product warranties with various terms ranging from one year from the date of first use or 18 months for parts to 25 years for certain heat exchangers. The Company has an obligation to replace parts 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, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Warranty accrual:	*(in thousands)*			
Balance, beginning of period	$ 14,008	$ 13,160	$ 13,522	$ 12,652
Payments made	(1,825)	(1,687)	(4,834)	(4,481)
Provisions	1,272	2,054	4,767	5,356
Balance, end of period	$ 13,455	$ 13,527	$ 13,455	$ 13,527
Warranty expense:	$ 1,272	$ 2,054	$ 4,767	$ 5,356

7. Accrued Liabilities

Accrued liabilities were comprised of the following:

	September 30, 2021	December 31, 2020
	(in thousands)	
Warranty	$ 13,455	$ 13,522
Due to representatives	8,006	8,296
Payroll	8,770	8,155
Profit sharing	2,360	2,902
Worker's compensation	303	594
Medical self-insurance	1,574	1,546
Customer prepayments	5,296	5,067
Donations	370	570
Employee vacation time	3,747	3,321
Other	4,385	2,613
Total	$ 48,266	$ 46,586

8. Revolving Credit Facility

On July 26, 2021, the Company entered into a new revolving credit facility which provides for maximum borrowings of $30.0 million. Under the line of credit, there is one standby letter of credit totaling $1.8 million. Borrowings available under the revolving credit facility at September 30, 2021 were $28.2 million. Interest on borrowings is payable monthly at LIBOR plus 2.0%. The new revolving credit facility includes fallback language clearly defining an alternative reference rate which provides for specified replacement rates, as defined in the revolving credit facility agreement, upon a LIBOR cessation event. At the time of a LIBOR cessation event, the replacement rate self-executes without the need for negotiations or a formal amendment process. No fees are associated with the unused portion of the committed amount. The revolving credit facility expires on July 26, 2024.

We had no outstanding balance under our revolving credit facility at September 30, 2021 and December 31, 2020.

As of September 30, 2021, we were in compliance with our financial covenants related to the new revolving credit facility. These financial covenants require that we meet certain parameters related to our consolidated leverage ratio and our consolidated total liabilities to tangible net worth ratio. At September 30, 2021, our consolidated leverage ratio was 0.02 to 1 and met the requirement of being less than 2 to 1. Our consolidated total liabilities to tangible net worth ratio was 0.3 to 1, and met the requirement of being less than 2 to 1.

9. Income Taxes

The provision (benefit) for income taxes consists of the following:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(in thousands)			
Current	$ 4,508	$ 3,081	$ 8,498	$ 8,435
Deferred	19	2,615	2,766	7,676
Income tax provision	$ 4,527	$ 5,696	$ 11,264	$ 16,111

The provision for income taxes differs from the amount computed by applying the Federal statutory income tax rate before the provision for income taxes.

The reconciliation of the Federal statutory income tax rate to the effective income tax rate is as follows:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Federal statutory rate	21.0 %	21.0 %	21.0 %	21.0 %
State income taxes, net of Federal benefit	3.4	2.3	3.0	4.0
Excess tax benefits	(2.2)	(2.3)	(6.0)	(3.3)
Return to provision adjustments	0.6	0.5	—	0.2
Other	(0.3)	0.3	(0.4)	(0.8)
Effective tax rate	22.5 %	21.8 %	17.6 %	21.1 %

On May 21, 2021, the State of Oklahoma enacted House Bill 2960, effectively reducing the corporate income tax rate in Oklahoma from 6% to 4%. As a result of these changes, the Company adjusted its state deferred tax assets and liabilities in the second quarter of 2021 using the newly enacted rate for the periods when they are expected to be realized. This resulted in a benefit of $0.8 million included in the table above under State income taxes, net of Federal benefit, for the nine months ended September 30, 2021.

During the nine months ended September 30, 2021, the Company recorded an excess tax benefit of $3.8 million as compared to $2.5 million during the same period in 2020, an increase of 54%. The increase was primarily due to timing of stock option exercises as a result of our high stock price during the three months ended March 31, 2021.

We earn investment tax credits from the state of Oklahoma’s manufacturing property investment program. We use the flow-through method to account for investment tax credits earned on eligible tangible asset expenditures. Under this method, the investment tax credits are recognized as a reduction to our Oklahoma income tax expense in the year they are used. As of September 30, 2021, we have investment tax credit carryforwards of approximately $3.7 million. These credits have estimated expirations ranging from the year 2036 through 2040.

The Company's estimated annual 2021 effective tax rate, excluding discrete events, is approximately 25%. We file income tax returns in the U.S., as well as various state and foreign income tax returns jurisdictions. We are subject to U.S. income tax examinations for tax years 2017 to present, and to non-U.S. income tax examinations for the tax years 2016 to present. In addition, we are subject to state and local income tax examinations for the tax years 2016 to present. The Company continues to evaluate its need to file returns in various state jurisdictions. Any interest or penalties would be recognized as a component of income tax expense.

Coronavirus Aid, Relief, and Economic Security Act

The Coronavirus Aid, Relief, and Economic Security Act (the “CARES Act”) was enacted on March 27, 2020, and includes a retroactive correction to the 2017 Tax Cuts and Jobs Act that allows for much faster depreciation of qualified improvement property that is placed in service after December 31, 2017. Under current rules, the calculation of depreciation or repair deductions for prior years can be recomputed and a one-time catch-up adjustment is allowed in the current tax year for missed deductions. The adjustment is the difference between depreciation or repair deductions claimed versus depreciation or repair deductions that could have been claimed by the end of the prior tax year and does not require amending any prior year tax returns. The Company completed the prior year adjustment and the current-year catch up with the 2019 tax return as filed in the fourth quarter of 2020 resulting in a increase to our deferred tax liability of $4.7 million. For tax years 2020 and forward, the Company includes this treatment for our qualified property placed in service.

American Rescue Plan Act

On March 11, 2021, the American Rescue Plan Act (the “ARPA”) was enacted and signed into law. The ARPA is an economic stimulus package in response to the COVID-19 pandemic, which contains tax provisions that did not have a material impact to our consolidated financial statements. In accordance with accounting standards for income taxes, the impact of this new tax legislation was taken into account in the first quarter of 2021, the period in which it was enacted.

10. Share-Based Compensation

On May 22, 2007, our stockholders adopted a Long-Term Incentive Plan (“LTIP”) which provided an additional 3.3 million shares that could be granted in the form of stock options, stock appreciation rights, restricted stock awards, performance units and performance awards, in addition to the shares from the previous plan, the 1992 Plan. Under the LTIP, the exercise price of shares granted could not be less than 100% of the fair market value at the date of the grant.

On May 24, 2016, our stockholders adopted the 2016 Long-Term Incentive Plan (as amended, the "2016 Plan") which provides for approximately 8.9 million shares, comprised of 3.4 million new shares provided for under the 2016 Plan, approximately 0.4 million shares that were available for issuance under the previous LTIP that are now authorized for issuance under the 2016 Plan, approximately 2.6 million shares that were approved by the stockholders on May 15, 2018, and an additional 2.5 million shares that were approved by the stockholders on May 12, 2020. Under the 2016 Plan, shares can be granted in the form of stock options, stock appreciation rights, restricted stock awards, performance awards, dividend equivalent rights, and other awards. Under the 2016 Plan, the exercise price of shares granted may not be less than 100% of the fair market value at the date of the grant. The 2016 Plan is administered by the Compensation Committee of the Board of Directors or such other committee of the Board of Directors as is designated by the Board of Directors (the “Committee”). Membership on the Committee is limited to independent directors. The Committee determines the persons to whom awards are to be made, the type, size and terms of awards, interprets the 2016 Plan, establishes and revises rules and regulations relating to the 2016 Plan and makes any other determinations that it believes necessary for the administration of the 2016 Plan. The Committee may delegate certain duties to one or more officers of the Company as provided in the 2016 Plan.

Options

The total pre-tax compensation cost related to unvested stock options not yet recognized as of September 30, 2021 is $19.5 million and is expected to be recognized over a weighted average period of approximately 2.5 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, 2021 and 2020 using a Black Scholes-Merton Model:

	Nine months ended	
	September 30, 2021	**September 30, 2020**
Directors and SLT[1]:		
Expected dividend rate	$0.38	$0.33
Expected volatility	35.78%	31.63%
Risk-free interest rate	0.51%	0.64%
Expected life (in years)	4.0	5.0
Employees:		
Expected dividend rate	$0.38	$0.32
Expected volatility	38.69%	31.31%
Risk-free interest rate	0.30%	0.68%
Expected life (in years)	3.0	5.0

[1] Senior Leadership Team ("SLT") consists of officers and key members of management.

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, 2021:

Range of Exercise Prices	Number of Shares	Weighted Average Remaining Contractual Life *(in years)*	Weighted Average Exercise Price	Intrinsic Value *(in thousands)*
$ 8.17 - $ 40.87	593,901	4.88	$ 30.33	$ 20,790
$ 41.37 - $ 41.37	415,541	6.72	41.37	9,961
$ 42.42 - $ 73.36	139,605	8.36	45.08	2,828
Total	1,149,047	5.97	$ 36.12	$ 33,579

The following is a summary of stock options vested and exercisable as of September 30, 2020:

Range of Exercise Prices	Number of Shares	Weighted Average Remaining Contractual Life *(in years)*	Weighted Average Exercise Price	Intrinsic Value *(in thousands)*
$ 7.18 - $ 36.95	526,235	5.51	$ 28.03	$ 16,957
$ 37.00 - $ 40.87	1,978	7.34	38.50	43
$ 41.37 - $ 60.32	210,496	8.19	41.53	3,940
Total	738,709	6.28	$ 31.90	$ 20,940

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

Stock Options	Shares	Weighted Average Exercise Price
Outstanding at December 31, 2020	3,752,945	$ 39.00
Granted	360,980	72.93
Exercised	(412,284)	35.35
Forfeited or Expired	(140,077)	48.51
Outstanding at September 30, 2021	3,561,564	$ 42.49
Exercisable at September 30, 2021	1,149,047	$ 36.12

The total intrinsic value of options exercised during the nine months ended September 30, 2021 and 2020 was $15.1 million and $12.1 million, respectively. The cash received from options exercised during the nine months ended September 30, 2021 and 2020 was $14.6 million and $18.5 million, respectively. The impact of these cash receipts is included in financing activities in the accompanying Consolidated Statements of Cash Flows.

Performance Awards

We have awarded performance restricted stock units ("PSUs") to certain officers and key employees under our 2016 Plan. Unlike our restricted stock awards, these PSUs are not considered legally outstanding and do not accrue dividends during the vesting period. These PSUs vest based on the level of achievement with respect to the Company's three year total shareholder return ("TSR") benchmarked against similar companies included in the capital goods sector of the S&P SmallCap 600 Index. The TSR measurement period is the three years ending December 31, 2023. At the end of the measurement period, each award will be converted into common stock at 0% to 200% of the PSUs held, depending on overall TSR as compared to the S&P SmallCap 600 Index benchmark companies.

The total pre-tax compensation cost related to unvested PSUs not yet recognized as of September 30, 2021 is $1.1 million and is expected to be recognized over a weighted average period of approximately 2.2 years.

The following weighted average assumptions were used to determine the fair value of the PSUs granted on the original grant date for expense recognition purposes for PSUs granted during the nine months ended September 30, 2021 using a Monte Carlo Model:

	Nine months ended September 30, 2021
Expected dividend rate	$0.38
Expected volatility	39.10%
Risk-free interest rate	0.28%
Expected life (in years)	2.60

The expected term of the PSUs is based on the remaining performance period ending December 31, 2023. 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.

A summary of the unvested PSUs is as follows:

	Shares	Weighted Average Grant Date Fair Value
Unvested at December 31, 2020	—	$ —
Granted	18,483	87.78
Vested	—	—
Forfeited	(1,632)	87.78
Unvested at September 30, 2021	16,851	$ 87.78

Restricted Stock

The fair value of restricted stock awards is based on the fair market value of AAON, Inc. common stock on the respective grant dates, reduced for the present value of dividends. At September 30, 2021, unrecognized compensation cost related to unvested restricted stock awards was approximately $4.8 million, which is expected to be recognized over a weighted average period of approximately 2.3 years.

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

	Shares	Weighted Average Grant Date Fair Value
Unvested at December 31, 2020	224,691	$ 38.22
Granted	32,600	69.12
Vested	(89,523)	35.85
Forfeited	(7,051)	49.81
Unvested at September 30, 2021	160,717	$ 45.29

Share-Based Compensation

A summary of share-based compensation is as follows:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Grant date fair value of awards during the period:		*(in thousands)*		
Options	$ 152	$ 258	$ 6,870	$ 12,332
Performance awards	32	—	1,622	—
Restricted stock	80	—	2,253	3,316
Total	$ 264	$ 258	$ 10,745	$ 15,648
Share-based compensation expense:				
Options	$ 2,167	$ 2,208	$ 6,594	$ 6,136
Performance awards	166	—	355	—
Restricted stock	658	644	1,835	2,410
Total	$ 2,991	$ 2,852	$ 8,784	$ 8,546
Income tax benefit/(deficiency) related to share-based compensation:				
Options	$ 440	$ 579	$ 3,010	$ 1,990
Restricted stock	1	9	820	503
Total	$ 441	$ 588	$ 3,830	$ 2,493

Share-based compensation expense is recognized on a straight-line basis over the service period of the related stock options and restricted stock awards. Historically, stock options and restricted stock awards, granted to employees, vest at a rate of 20% per year. Restricted stock awards granted to directors historically vest one-third each year or, if granted on or after May 2019, vest over the shorter of directors' remaining elected term or one-third each year. As of March 2021, all new grants of stock options and restricted stock awards, granted to employees, vest at a rate of 33.3% per year. Forfeitures are accounted for as they occur.

Historically, if the employee or director is retirement eligible (as defined by the applicable LTIP or 2016 Plan) or becomes retirement eligible during service period of the related stock options and restricted stock award, the service period (and compensation expense recognition) is the lesser of 1) the grant date, if retirement eligible on grant date, or 2) the period between grant date and retirement eligible date. All stock options and restricted stock awards granted on or after March 1, 2020 to retirement eligible employees or directors contain a one-year employment requirement (minimum service period) or the entire award is forfeited.

Share-based compensation expense is recognized on a straight-line basis over the service period of the performance awards. The performance awards cliff vest at the end of the performance period. The performance awards are subject to several service conditions and market conditions, as defined by the performance restricted stock unit agreement, which allows the holder to retain a pro-rata amount of awards as a result of certain termination conditions, retirement, change in common control or death. Forfeitures are accounted for as they occur.

11. Employee Benefits

Defined Contribution Plan - 401(k)

We sponsor a defined contribution plan (the “Plan”). Eligible employees may make contributions in accordance with the Plan and IRS guidelines. In addition to the traditional 401(k), eligible employees are given the option of making an after-tax contribution to a Roth 401(k) or a combination of both. The Plan provides for automatic enrollment and for an automatic increase to the deferral percentage at January 1st of each year and each year thereafter. Eligible employees are automatically enrolled in the Plan at a 6% deferral rate and currently contributing employees deferral rates will be increased to 6% unless their current rate is above 6% or the employee elects to decline the automatic enrollment or increase. Administrative expenses are paid for by Plan participants. The Company paid no administrative expenses during the nine months ended September 30, 2021 and 2020.

The Company matches 175%, up to 6%, of employee contributions of eligible compensation in Company stock. The Company match vests over six years, with 20% vesting each year after two years of service. Additionally, Plan participant forfeitures are used to reduce the cost of the Company contributions.

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(in thousands)			
Contributions, net of forfeitures, made to the defined contribution plan	$ 2,526	$ 2,242	$ 6,924	$ 6,791

Profit Sharing Bonus Plan

We maintain a discretionary profit sharing bonus plan under which approximately 10% of pre-tax profit is paid to eligible employees on a quarterly basis in order to reward employee productivity. Eligible employees are regular full-time employees who are actively employed and working on the first and last days of the calendar quarter and who were employed full-time for at least three full months prior to the beginning of the calendar quarter, excluding the Company's SLT.

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(in thousands)			
Profit sharing bonus plan expense	$ 2,358	$ 3,000	$ 7,409	$ 8,691

Employee Medical Plan

We self-insure for our employees' health insurance. Eligible employees are regular full-time employees who are actively employed and working. Participants are expected to pay a portion of the premium costs for coverage of the benefits provided under the Plan. We estimate our self-insurance liabilities using an analysis provided by our claims administrator and our historical claims experience. In addition, the Company matches 175% of a participating employee's allowed contributions to a qualified health saving account to assist employees with our health insurance plan deductibles.

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(in thousands)			
Medical claim payments	$ 2,342	$ 2,985	$ 6,188	$ 6,843
Health saving account contributions	888	890	2,621	2,663

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, restricted stock awards and performance restricted stock units.

The following table sets forth the computation of basic and diluted earnings per share:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
Numerator:	*(in thousands, except share and per share data)*			
Net income	$ 15,581	$ 20,460	$ 52,572	$ 60,117
Denominator:				
Basic weighted average shares	52,420,711	52,260,551	52,392,300	52,174,705
Effect of dilutive stock options, restricted stock and performance awards	1,125,802	890,744	1,272,697	780,344
Diluted weighted average shares	53,546,513	53,151,295	53,664,997	52,955,049
Earnings per share:				
Basic	$ 0.30	$ 0.39	$ 1.00	$ 1.15
Diluted	$ 0.29	$ 0.38	$ 0.98	$ 1.14
Anti-dilutive shares:				
Shares	375,428	118,832	291,236	473,295

13. Stockholders’ Equity

Stock Repurchases

The Board has authorized three stock repurchase programs for the Company. The Company may purchase shares on the open market from time to time, up to a total of 5.7 million shares. The Board must authorize the timing and amount of these purchases and all repurchases are in accordance with the rules and regulations of the SEC allowing the Company to repurchase shares from the open market.

Our open market repurchase programs are as follows:

Effective Date	Authorized Repurchase $	Expiration Date
May 16, 2018 [1]	$15 million	March 1, 2019
March 5, 2019 [1]	$20 million	March 4, 2020
March 13, 2020	$20 million	** [2]

[1] The 2018 and 2019 purchase authorizations were executed under 10b5-1 programs.

[2] Expiration Date is at Board's discretion. The Company is authorized to effectuate repurchases of the Company's common stock on terms and conditions approved in advance by the Board.

The Company also has a stock repurchase arrangement by which employee-participants in our 401(k) savings and investment plan are entitled to have shares of AAON, Inc. stock in their accounts sold to the Company. The maximum number of shares to be repurchased is contingent upon the number of shares sold by employee-participants.

Lastly, the Company repurchases shares of AAON, Inc. stock from certain of its directors and employees for payment of statutory tax withholdings on stock transactions. All other repurchases from directors or employees are contingent upon Board approval. All repurchases are done at current market prices.

Our repurchase activity is as follows:

	Nine Months Ended					
	September 30, 2021			September 30, 2020		
	(in thousands, except share and per share data)					
Program	**Shares**	**Total $**	**$ per share**	**Shares**	**Total $**	**$ per share**
Open market	—	$ —	$ —	103,689	$ 4,987	$ 48.10
401(k)	220,336	15,014	68.14	303,112	16,403	54.12
Directors and employees	21,779	1,537	70.57	22,655	1,130	49.88
Total	242,115	$ 16,551	$ 68.36	429,456	$ 22,520	$ 52.44

Our repurchase activity since Company inception, including our current authorized stock repurchase programs, are as follows:

	Inception to September 30, 2021		
	(in thousands, except share and per share data)		
Program	**Shares**	**Total $**	**$ per share**
Open market	4,205,255	$ 74,793	$ 17.79
401(k)	8,126,996	160,014	19.69
Directors and employees	2,026,980	22,288	11.00
Total	14,359,231	$ 257,095	$ 17.90

Subsequent to September 30, 2021 and through November 1, 2021, the Company repurchased 19,545 shares for $1.3 million from our 401(k) savings and investment plan.

Dividends

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

Our recent dividends are as follows:

Declaration Date	Record Date	Payment Date	Dividend per Share
May 15, 2020	June 3, 2020	July 1, 2020	$0.19
November 10, 2020	November 27, 2020	December 18, 2020	$0.19
May 17, 2021	June 3, 2021	July 1, 2021	$0.19

14. New Markets Tax Credit

On October 24, 2019, the Company entered into a transaction with a subsidiary of an unrelated third-party financial institution (the "Investor") and a certified Community Development Entity under a qualified New Markets Tax Credit ("NMTC") program pursuant to Section 45D of the Internal Revenue Code of 1986, as amended, related to an investment in plant and equipment to facilitate the expansion of our Longview, Texas manufacturing operations (the "Project"). In connection with the NMTC transaction, the Company received a $23.0 million NMTC allocation for the Project and secured low interest financing and the potential for future debt forgiveness related to the Project.

Upon closing of the NMTC transaction, the Company provided an aggregate of approximately $15.9 million to the Investor, in the form of a loan receivable, with a term of twenty-five years, bearing an interest rate of 1.0%. This $15.9 million in proceeds plus capital contributed from the Investor was used to make an aggregate $22.5 million loan to a subsidiary of the Company. This financing arrangement is secured by equipment at the Company's Longview, Texas facilities and a guarantee from the Company, including an unconditional guarantee of NMTCs.

This transaction also includes a put/call feature that either of which can be exercised at the end of the seven-year compliance period. The Investor may exercise its put option or the Company can exercise the call, both of which could serve to trigger forgiveness of a portion of the debt. The Investor's interest of $6.3 million is recorded in New market tax credit obligation on the consolidated balance sheet. The Company incurred approximately $0.3 million of debt issuance costs related to the above transactions, which are being amortized over the life of the transaction.

The Investor is subject to 100 percent recapture of the NMTC it receives for a period of seven years, as provided in the Internal Revenue Code and applicable U.S. Treasury regulations in the event that the financing facility of the Borrower under the transaction (AAON Coil Products, Inc.) becomes ineligible for NMTC treatment per the Internal Revenue Code requirements. The Company is required to be in compliance with various regulations and contractual provisions that apply to the NMTC arrangement. Noncompliance with applicable requirements could result in the Investor's projected tax benefits not being realized and, therefore, require the Company to indemnify the Investor for any loss or recapture of the NMTC related to the financing until such time as the recapture provisions have expired under the applicable statute of limitations. The Company does not anticipate any credit recapture will be required in connection with this financing arrangement.

The Investor and its majority owned community development entity are considered VIEs and the Company is the primary beneficiary of the VIEs. Because the Company is the primary beneficiary of the VIEs, they have been included in the consolidated financial statements. There are no other assets, liabilities or transaction in these VIEs outside of the financing transactions executed as part of the NMTC arrangement.

15. Commitments and Contingencies

We are subject to various claims and legal actions that arise in the ordinary course of business. We closely monitor these claims and legal actions and frequently consult with our legal counsel to determine whether they may, when resolved, have a material adverse effect on our financial position, results of operations or cash flows and we accrue and/or disclose loss contingencies as appropriate. We have concluded that the likelihood is remote that the ultimate resolution of any pending litigation or claims will be material or have a material adverse effect on the Company's business, financial position, results of operations and/or cash flows.

We are occasionally party to short-term, cancellable and occasionally non-cancellable, fixed 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 derivative instruments because they meet the normal purchase and normal sales exemption. We had no material contractual purchase obligations as of September 30, 2021.

16. Related Parties

The Company purchases some supplies from an entity controlled by the Company's Executive Chairman. The Company sometimes makes sales to the Executive Chairman and CEO/President. Additionally, the Company sells units to an entity owned by a member of the CEO/President's immediate family. This entity is also one of the Company's Representatives and as such, the Company makes payments to the entity for Third Party Products.

The following is a summary of transactions and balance with affiliates:

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(in thousands)			
Sales to affiliates	$ 1,560	$ 662	$ 2,372	$ 2,550
Payments to affiliates	23	110	153	207

	September 30, 2021	December 31, 2020
	(in thousands)	
Due from affiliates	$ 544	$ 342
Due to affiliates	—	—

17. Segments

The following table summarizes certain financial data related to our segments. Transactions between segments are recorded based on prices negotiated between the segments. Sales of units represent the selling price of our units plus freight and other miscellaneous charges less any returns and allowances. Parts include sales of purchased and fabricated parts including our coils along with the related freight and less any returns and allowances. The "Other" category in the table below includes certain expenses that are not allocated to the reportable segments and are primarily engineering related expenses.

Asset information by segment is not easily identifiable or reviewed by the chief operating decision maker. As such, this information is not included below.

	Three Months Ended		Nine Months Ended	
	September 30, 2021	September 30, 2020	September 30, 2021	September 30, 2020
	(in thousands)			
Sales				
Units	$ 125,862	$ 123,827	$ 366,597	$ 372,267
Parts - External	12,977	11,222	32,369	26,162
Parts - Inter-segment	6,325	5,659	19,005	18,074
Other	(268)	(277)	(731)	(578)
Eliminations	(6,325)	(5,659)	(19,005)	(18,074)
Net sales	$ 138,571	$ 134,772	$ 398,235	$ 397,851
Gross Profit				
Units	$ 35,167	$ 41,675	$ 111,247	$ 128,523
Parts - External	5,072	4,917	12,385	11,641
Parts - Inter-segment	(366)	(758)	(527)	(1,587)
Other	(4,220)	(5,744)	(12,349)	(18,238)
Eliminations	366	758	527	1,587
Net gross profit	$ 36,019	$ 40,848	$ 111,283	$ 121,926

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, 2020.

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 SEC 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, 2020. 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 standard, semi-custom and custom rooftop units, chillers, packaged outdoor mechanical rooms, air handling units, makeup air units, energy recovery units, condensing units, geothermal/water-source heat pumps, coils, and controls. These products are marketed and sold to retail, manufacturing, educational, lodging, supermarket, medical and other commercial industries. We market our products to all 50 states in the United States and all provinces in Canada. Foreign sales were approximately $11.0 million of our total net sales for the nine months just ended and $8.4 million of our sales during the same period of 2020.

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 uncertainty of the economy has negatively impacted the commercial and industrial new construction markets. A further decline in economic activity could result in a decrease in 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. The 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 six 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. Our sales strategy is currently balanced between new construction and replacement applications. The new construction market through the third quarter of 2021 has improved compared to 2020. We continue to emphasize the benefits of AAON equipment to property owners in the replacement market.

Our manufacturing operations are considered a critical infrastructure industry, as defined by the U.S. Department of Homeland Security, as such, the decrees issued by national, state, and local governments in response to the COVID-19 pandemic have had minimal impact on our operations except for isolated higher employee absenteeism, especially in June 2020, in our manufacturing facilities. Our Longview, TX facility suffered from COVID-19 related absenteeism in the quarter ending September 30, 2021, which reduced the production of coils that were needed to complete units at our Tulsa, OK facility. We maintained continuous operations during the nine months ended September 30, 2021 except for the shutdown for planned maintenance in January 2021 and the February 2021 weather related event described in Note 1. For the most part, our workers are able to socially distance themselves during the manufacturing process. Additional precautions have been taken to social distance workers that work in close environments and we have facilitated voluntary on-site COVID-19 vaccine clinics. The Company utilizes sanitation stations and performs additional cleaning and sanitation throughout the day.

While the Company's operations are primarily in Oklahoma and Texas, our domestic sales to customers cover almost all 50 states. Only the state of Texas is responsible for more than 10% of our revenues. Because we have managed to maintain almost continuous operations with reasonable lead times through 2020 and 2021, our order intake is strong and has increased throughout 2021 as the economy has opened back up and COVID-19 restrictions have lessened. We expect to increase our production for the remainder of 2021 and into 2022.

The Architecture Billings Index ("ABI") was down for most of 2020, indicating a decline in construction, which started to impact the new nonresidential construction market in late 2020. This slightly impacted the Company with a slower order intake level and caused us to slow down some of our production in the beginning of the first quarter 2021. Beginning in February 2021, the ABI index began a historic rebound with the May and June 2021 ABI Index being two of the highest scores in the index's 25-year history. While the ABI did start to decline in June and July, August and September were two straight months of increases.

Even if new construction declines, our equipment is uniquely positioned to address COVID-19 challenges by providing heightened filtration and sanitation through the use of MERV 13 filters, UV lights and bi-polar ionization installed in the factory. With approximately 50% of our total sales already represented by the replacement market, we are confident of our ability to grow our market share in the replacement market while we continue to pursue opportunities in the new construction market.

We had unrestricted cash and cash equivalents of $101.8 million as of September 30, 2021. Our capital expenditures during the nine months ended September 30, 2021 were $42.6 million, as compared to $49.0 million for the same period a year ago, and we anticipate our full-year 2021 capital expenditures will total approximately $60.0 million. The expansion of our Longview, Texas facility was completed and operational during the first quarter 2021. The Company also has $28.2 million available under its line of credit.

Additionally, we continue to experience challenges in a tight labor market, especially the hiring of both skilled and unskilled production labor. In July 2021, we increased starting wages for our production workforce by 7.0%. We also have put a cost of living increase of 3.5% in place in October for all employees below the Director level. We will continue to implement human resource initiatives to retain and attract labor to further improve productivity and production efficiencies.

The principal components of cost of goods sold are labor, raw materials, component costs, factory overhead, freight and engineering expense. The principal high volume raw materials used in our manufacturing processes are steel, copper, and aluminum, and are obtained from domestic suppliers. We also purchase from domestic manufacturers certain components, including compressors, motors, and electrical controls. Although, we have experienced some supply chain challenges, due to our strong vendor relationships as well as our favorable liquidity position, we have experienced minimal disruption to our supply chain due to COVID-19. While our supply chain disruptions to date have been minimal and intermittent, they have impacted the production process which creates inefficiencies and can deteriorate our profit margins.

The price levels of most raw materials were stable prior to 2020, but we continue to see increases in raw material costs which we are managing through price increases to counteract their impact. There is also a possibility prices could rise in the future depending on the impact COVID-19 and subsequent inflation has on our supply chain. At September 30, 2021, the price (twelve month trailing average) for copper, galvanized steel, stainless steel and aluminum increased 38.3%, 79.5%, 39.8%, and 56.7%, respectively, as compared to the price (twelve month trailing average) at September 30, 2020. We anticipate that the average cost of raw materials and certain components purchased, including the impact of rising inflation and tariffs, for the remainder of 2021 will be higher than the costs experienced during the year ended December 31, 2020.

We attempt to limit the impact of price fluctuations on these materials by entering into cancellable and non-cancellable fixed price contracts with our major suppliers for periods of six to 18 months. We expect to receive delivery of raw materials from our fixed price contracts for use in our manufacturing operations.

The following are recent highlights and items that impacted our results of operations, cash flows and financial condition:

- Our backlog is at a record level, 144% higher than it was at December 31, 2020 due to our reasonable lead times and quality products.

- Our third quarter 2021 results demonstrated a positive performance, despite the external challenges, with sales increasing approximately 2.8% for the three months ended as compared to the same period last year.

- Bookings increased approximately 60% in the third quarter of 2021 compared to 2020 indicating an improved demand for our products as well as increase in orders in advance of our announced September 2021 price increases.

- Our warranty expense decreased 38% in the third quarter of 2021 compared to 2020 as a result of the quality control efforts the Company has put in place in the past few years.

Backlog

The following table shows our historical backlog levels:

September 30, 2021	December 31, 2020	September 30, 2020
	(in thousands)	
$ 181,813	$ 74,417	$ 84,885

The Company started 2020 with a high backlog due to challenges maintaining adequate sheet-metal production capacity in 2019. The Company started to increase its sheet-metal production capacity at the end of 2019 and into 2020 with the addition of new Salvagnini machines. This led in part to all time record sales and earnings for the year-ended December 31, 2020 that helped reduce our backlog at the end of 2020. In 2021, as a result of our decreased lead time, increase in demand, and increase in orders in advance of our announced June 1, 2021 and September 1, 2021 price increase, bookings increased approximately 60% in the third quarter of 2021 compared to 2020.

Results of Operations

Three months ended September 30, 2021 vs. Three months ended September 30, 2020

Units Sold

	Three Months Ended	
	September 30, 2021	September 30, 2020
Rooftop units	3,746	4,372
Condensing units	560	593
Air handlers	646	534
Outdoor mechanical rooms	2	6
Water source heat pumps	1,576	1,847
Total Units	6,530	7,352

Net Sales

	Three Months Ended			
	September 30, 2021	September 30, 2020	Change	% Change
	(in thousands, except unit data)			
Net sales	$ 138,571	$ 134,772	$ 3,799	2.8 %
Total units	6,530	7,352	(822)	(11.2)%

While the third quarter of 2021 benefited from an increased demand, challenges hiring additional production labor hindered our ability to produce at the same capacity during the three months ended September 30, 2021 as compared to September 30, 2020. This resulted in an 11.2% decrease in total units sold, mostly related to our rooftop units. The quarter benefited from our January and June 2021 price increases, which realized approximately a 5.0% increase in sales in the period. Our parts sales were also up 15% for the quarter that helped increase our net sales for the period.

Cost of Sales

	Three Months Ended		Percent of Sales	
	September 30, 2021	September 30, 2020	2021	2020
	(in thousands)			
Cost of sales	$ 102,552	$ 93,924	74.0 %	69.7 %
Gross profit	36,019	40,848	26.0 %	30.3 %

The principal components of cost of sales 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 increase in raw material costs were approximately 6.9% of sales for the quarter which were not completely offset by the realization of price increases we put in place during the year. The tightening labor market has caused us to also implement raises in entry level wages ahead of realizing our price increases. The reduction in overall unit production, due to challenges hiring additional production labor, resulted in unfavorable labor and overhead inefficiencies, including the Company's ability to absorb certain fixed costs. Lastly, the small disruptions to our production schedule from supply chain delays negatively impacted our production efficiency. All of these factors resulted in a decrease in gross profit during the three months ended September 30, 2021 as compared to 2020.

Twelve-month average raw material cost per pound as of September 30:

	2021	2020	% Change
Copper	$ 4.95	$ 3.58	38.3 %
Galvanized steel	$ 0.79	$ 0.44	79.5 %
Stainless steel	$ 1.79	$ 1.28	39.8 %
Aluminum	$ 1.88	$ 1.20	56.7 %

Selling, General and Administrative Expenses

	Three Months Ended		Percent of Sales	
	September 30, 2021	September 30, 2020	2021	2020
	(in thousands)			
Warranty	$ 1,272	$ 2,054	0.9 %	1.5 %
Profit sharing	2,358	3,000	1.7 %	2.2 %
Salaries & benefits	6,029	4,725	4.4 %	3.5 %
Stock compensation	1,418	1,330	1.0 %	1.0 %
Advertising	225	229	0.2 %	0.2 %
Depreciation	645	515	0.5 %	0.4 %
Insurance	733	254	0.5 %	0.2 %
Professional fees	851	542	0.6 %	0.4 %
Donations	97	106	0.1 %	0.1 %
Bad debt expense	(12)	117	— %	0.1 %
Other	2,281	1,844	1.6 %	1.4 %
Total SG&A	$ 15,897	$ 14,716	11.5 %	10.9 %

The Company's warranty expense continues to improve after making significant quality control improvements in the past two years. Profit sharing expenses decreased due to our decreased earnings for the period. Salaries and benefits are up due to increases in bonuses and employee incentives.

Income Taxes

	Three Months Ended		Effective Tax Rate	
	September 30, 2021	September 30, 2020	2021	2020
	(in thousands)			
Income tax provision	$ 4,527	$ 5,696	22.5 %	21.8 %

The Company’s estimated annual 2021 effective tax rate, excluding discrete events, is expected to be approximately 25%. The effective rate is lower than our estimated rate due to the impact related to excess tax benefits.

Nine Months Ended September 30, 2021 vs. Nine Months Ended September 30, 2020

Units Sold

	Nine Months Ended	
	September 30, 2021	September 30, 2020
Rooftop units	11,362	12,179
Condensing units	1,696	1,447
Air handlers	1,846	1,545
Outdoor mechanical rooms	22	22
Water source heat pumps	5,108	5,109
Total Units	20,034	20,302

Net Sales

	Nine Months Ended			
	September 30, 2021	September 30, 2020	Change	% Change
	(in thousands, except unit data)			
Net sales	$ 398,235	$ 397,851	$ 384	0.1 %
Total units	20,034	20,302	(268)	(1.3)%

In 2021, the Company lost production days in January for planned maintenance and in February due to impacts of bad weather. While the second and third quarter of 2021 benefited from an increasing demand, challenges hiring additional production labor hindered our ability to produce units at the same capacity in 2020. Although overall units sold decreased approximately 1.3% for the nine months ended September 30 2021 vs 2020, sales increased 0.1% due primarily to our January 2021 price increase. The Company's June price increase has been slower to realize given our large backlog and slightly longer lead times.

Cost of Sales

	Nine Months Ended		Percent of Sales	
	September 30, 2021	September 30, 2020	2021	2020
	(in thousands)			
Cost of sales	$ 286,952	$ 275,925	72.1 %	69.4 %
Gross profit	111,283	121,926	27.9 %	30.6 %

The principal components of cost of sales 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. We continue to see overall raw material costs increase. In addition, reduction in overall unit production due to challenges hiring additional production labor, resulting in unfavorable labor and overhead inefficiencies, including the Company's ability to absorb certain fixed costs. Combined with the increase in overall raw material costs, this resulted in an overall decrease in gross profit during the nine months ended September 30, 2021 as compared to 2020.

Twelve-month average raw material cost per pound as of September 30:

	2021	2020	% Change
Copper	$ 4.95	$ 3.58	38.3 %
Galvanized steel	$ 0.79	$ 0.44	79.5 %
Stainless steel	$ 1.79	$ 1.28	39.8 %
Aluminum	$ 1.88	$ 1.20	56.7 %

Selling, General and Administrative Expenses

	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020	Percent of Sales 2021	Percent of Sales 2020
	(in thousands)			
Warranty	$ 4,767	$ 5,356	1.2 %	1.3 %
Profit sharing	7,409	8,691	1.9 %	2.2 %
Salaries & benefits	17,088	14,921	4.3 %	3.8 %
Stock compensation	4,077	4,020	1.0 %	1.0 %
Advertising	692	446	0.2 %	0.1 %
Depreciation	1,979	1,470	0.5 %	0.4 %
Insurance	2,194	733	0.6 %	0.2 %
Professional fees	2,258	1,796	0.6 %	0.5 %
Donations	323	1,892	0.1 %	0.5 %
Bad debt expense	(29)	193	— %	— %
Other	6,730	6,351	1.7 %	1.6 %
Total SG&A	$ 47,488	$ 45,869	11.9 %	11.5 %

Profit sharing expenses decreased due to our decreased earnings for the period. Salaries and benefits are up slightly due to increases in bonuses, severance payouts and employee incentives. Insurance expense increased due to an increase in overall premiums during the period.

Income Taxes

	Nine Months Ended September 30, 2021	Nine Months Ended September 30, 2020	Effective Tax Rate 2021	Effective Tax Rate 2020
	(in thousands)			
Income tax provision	$ 11,264	$ 16,111	17.6 %	21.1 %

The Company’s estimated annual 2021 effective tax rate, excluding discrete events, is expected to be approximately 25%. The nine months ended September 30, 2021 had a lower tax rate, compared to 2020, due to an increase in our excess tax benefit related to stock awards of $1.3 million or 54%. The increase was primarily due to timing of stock awards as a result of our high stock price during the three months ended March 31, 2021. In addition, in May 2021, the State of Oklahoma reduced corporate tax rate from 6% to 4%. As a result of these changes, the Company adjusted its state deferred tax assets and liabilities in the second quarter of 2021 using the newly enacted rate for the periods when they are expected to be realized.

Liquidity and Capital Resources

Our working capital and capital expenditure requirements are generally met through net cash provided by operations and the occasional use of the revolving bank line of credit based on our current liquidity at the time.

Working Capital - Our unrestricted cash increased $22.8 million from December 31, 2020 to September 30, 2021 and totaled $101.8 million at September 30, 2021.

Revolving Line of Credit - Under the revolving credit facility, there was one standby letter of credit of $1.8 million as of September 30, 2021. At September 30, 2021, we have $28.2 million of borrowings available under the revolving credit facility. 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, 2021 and December 31, 2020. Interest on borrowings is payable monthly at LIBOR plus 2.0%.

As of September 30, 2021, we were in compliance with our financial covenants related to the revolving credit facility. These financial covenants require that we meet certain parameters related to our consolidated leverage ratio and our consolidated total liabilities to tangible net worth ratio. At September 30, 2021, our consolidated leverage ratio was 0.02 to 1 and met the requirement of being less than 2 to 1. Our consolidated total liabilities to tangible net worth ratio was 0.3 to 1, and met the requirement of being less than 2 to 1.

New Market Tax Credit Obligation - On October 24, 2019, the Company entered into a transaction with a subsidiary of an unrelated third-party financial institution (the “Investor”) and a certified Community Development Entity under a qualified New Markets Tax Credit (“NMTC”) program pursuant to Section 45D of the Internal Revenue Code of 1986, as amended, related to an investment in plant and equipment to facilitate the expansion of our Longview, Texas manufacturing operations (the “Project”). In connection with the NMTC transaction, the Company received a $23.0 million NMTC allocation for the Project and secured low interest financing and the potential for future debt forgiveness related to the expansion of its Longview, Texas facilities.

Upon closing of the NMTC transaction, the Company provided an aggregate of approximately $15.9 million to the Investor, in the form of a loan receivable, with a term of twenty-five years, bearing an interest rate of 1.0%. This $15.9 million in proceeds plus capital contributed from the Investor was used to make an aggregate $22.5 million loan to a subsidiary of the Company. This financing arrangement is secured by equipment at the Company's Longview, Texas facilities, and a guarantee from the Company, including an unconditional guarantee of NMTCs.

Stock Repurchases - The Board has authorized three stock repurchase programs for the Company. The Company may purchase shares on the open market from time to time, up to a total of 5.7 million shares. The Board must authorize the timing and amount of these purchases and all repurchases are in accordance with the rules and regulations of the SEC allowing the Company to repurchase shares from the open market.

Our open market repurchase programs are as follows:

Effective Date	Authorized Repurchase $	Expiration Date
May 16, 2018 [1]	$15 million	March 1, 2019
March 5, 2019 [1]	$20 million	March 4, 2020
March 13, 2020	$20 million	** [2]

[1] The 2018 and 2019 purchase authorizations were executed under 10b5-1 programs.

[2] Expiration Date is at Board's discretion. The Company is authorized to effectuate repurchases of the Company's common stock on terms and conditions approved in advance by the Board.

The Company also has a stock repurchase arrangement by which employee-participants in our 401(k) savings and investment plan are entitled to have shares of AAON, Inc. stock in their accounts sold to the Company. The maximum number of shares to be repurchased is contingent upon the number of shares sold by employee-participants.

Lastly, the Company repurchases shares of AAON, Inc. stock from certain of its directors and employees for payment of statutory tax withholdings on stock transactions. All other repurchases from directors or employees are contingent upon Board approval. All repurchases are done at current market prices.

Our repurchase activity is as follows:

	Nine Months Ended					
	September 30, 2021			September 30, 2020		
	(in thousands, except share and per share data)					
Program	Shares	Total $	$ per share	Shares	Total $	$ per share
Open market	—	$ —	$ —	103,689	$ 4,987	$ 48.10
401(k)	220,336	15,014	68.14	303,112	16,403	54.12
Directors and employees	21,779	1,537	70.57	22,655	1,130	49.88
Total	242,115	$ 16,551	$ 68.36	429,456	$ 22,520	$ 52.44

Our repurchase activity since Company inception, including our current authorized stock repurchase programs, are as follows:

	Inception to September 30, 2021		
	(in thousands, except share and per share data)		
Program	Shares	Total $	$ per share
Open market	4,205,255	$ 74,793	$ 17.79
401(k)	8,126,996	160,014	19.69
Directors and employees	2,026,980	22,288	11.00
Total	14,359,231	$ 257,095	$ 17.90

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

Our recent dividends are as follows:

Declaration Date	Record Date	Payment Date	Dividend per Share
May 15, 2020	June 3, 2020	July 1, 2020	$0.19
November 10, 2020	November 27, 2020	December 18, 2020	$0.19
May 17, 2021	June 3, 2021	July 1, 2021	$0.19

Based on historical performance and current expectations, we believe our cash and cash equivalents balance, the projected cash flows generated from our operations, our existing committed revolving credit facility (or comparable financing) and our expected ability to access capital markets will satisfy our working capital needs, capital expenditures and other liquidity requirements associated with our operations in 2021 and the foreseeable future.

Statement of Cash Flows

The following table reflects the major categories of cash flows for the nine months ended September 30, 2021 and 2020. For additional details, see the consolidated financial statements.

	Nine Months Ended	
	September 30, 2021	September 30, 2020
	(in thousands)	
Operating Activities		
Net Income	$ 52,572	$ 60,117
Income statement adjustments, net	34,456	37,131
Changes in assets and liabilities:		
Accounts receivable	(11,369)	5,011
Income taxes	2,588	(3,142)
Inventories	(22,712)	(6,994)
Prepaid expenses and other	937	(598)
Accounts payable	16,390	3,654
Deferred revenue	316	1,128
Accrued liabilities & donations	1,525	688
Net cash provided by operating activities	74,703	96,995
Investing Activities		
Capital expenditures	(42,636)	(48,955)
Other	60	99
Net cash used in investing activities	(42,576)	(48,856)
Financing Activities		
Stock options exercised	14,573	18,519
Repurchase of stock	(15,014)	(21,390)
Employee taxes paid by withholding shares	(1,537)	(1,130)
Cash dividends paid to stockholders	(9,964)	(9,910)
Net cash used in financing activities	$ (11,942)	$ (13,911)

Cash Flows Provided by Operating Activities

The Company manages cash needs through working capital rather than drawing on its line of credit. Collections and payments cycles are on a normal pattern and fluctuate due to timing of receipts and payments. The Company has been able to improve its collections of outstanding receivables due in part through prepayment of orders. The decrease in cash flows from receivables was due to the increase in sales in the third quarter of 2021 and due to the lower overall accounts receivable at December 31, 2020, as a result of the planned Company shutdown during the last week of December 2020. The decrease in cash flows from inventory and increase in cash flows from accounts payable is due the increased raw materials pricing and timing of payments. The Company strategically purchases inventory to take advantage of favorable pricing and also to minimize future supply chain disruptions.

Cash Flows Used in Investing Activities

The capital expenditures for 2020 related primarily to the expansion of our Longview, Texas facility, which was completed and became operational during early 2021. Additionally, in 2020 we purchased Salvagnini sheet metal fabrication machines and completed our R&D lab as well as other operational improvements. The capital expenditure program for 2021 is estimated to be approximately $60.0 million. Many of these projects are subject to review and cancellation at the discretion of our CEO and Board of Directors without incurring substantial charges.

Cash Flows Used in Financing Activities

Stock options exercised fluctuate due to timing of employee exercises. The Company purchased approximately $5.0 million of our outstanding stock through the open market buyback program (Note 13) during the nine months ended September 30, 2020. There were no open market buybacks of our outstanding stock during the nine months ended September 30, 2021.

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

We had no material contractual purchase obligations as of September 30, 2021.

Critical Accounting Policies

There have been no material changes in the Company's critical accounting policies during the nine months ended September 30, 2021.

Recent Accounting Pronouncements

See Note 1 of the Notes to the Consolidated Financial Statements for a discussion of recent accounting pronouncements.

Forward-Looking Statements

This Quarterly Report on Form 10-Q includes "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as "expects", "anticipates", "intends", "plans", "believes", "seeks", "estimates", "will", "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, (4) general economic, market or business conditions, and (5) the impact of COVID-19 on the economy, demand for our products and our operations, including the measures taken by governmental authorities to address it, which may precipitate or exacerbate other risks and/or uncertainties.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Commodity Price Risk

We are exposed to volatility in the prices of commodities used in some of our products and we may use fixed price cancellable and non-cancellable contracts with our major suppliers for periods of six 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, 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.

(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.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

We are subject to various claims and legal actions that arise in the ordinary course of business. We closely monitor these claims and legal actions and frequently consult with our legal counsel to determine whether they may, when resolved, have a material adverse effect on our financial position, results of operations, or cash flows and we accrue and/or disclose loss contingencies as appropriate. We have concluded that the likelihood is remote that the ultimate resolution of any pending litigation or claims will be material or have a material adverse effect on the Company's business, financial position, results of operations or cash flows.

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, 2020. The risk factors described in our Annual Report could materially adversely affect our business, financial condition or future results. There have been no material changes to the risk factors included in our 2020 Annual Report except as noted below.

Risks Related to Governmental Regulation and Policies

Changes in legislation or government regulations or policies could adversely effect on our results of operations.

The sales, gross margins and profitability could be directly impacted by changes in legislation or government regulations or policies. Specifically, changes in environmental and energy efficiency standards and regulations related to global climate change are being implemented to curtail the use of hydrofluorocarbons which are used in refrigerants that are essential to many of our products. Our inability or delay in developing or marketing products that match customer demand while also meeting applicable efficiency and environmental standards may negatively impact our results.

Future legislation or regulations relating to environmental policies, product certification, product liability, taxes, amount and availability of tax incentives and other matters, may impact the results of each of our operating segments and our consolidated results.

Potential government imposed COVID-19 vaccine mandates could adversely affect our ability to attract and retain employees which could have a material adverse impact on our business and results of operations.

On September 9, 2021, President Biden directed the Department of Labor’s Occupational Safety and Health Administration ("OSHA") to issue an Emergency Temporary Standard requiring that all employers with at least 100 employees ensure that their employees are fully vaccinated for COVID-19 or require employees to obtain a negative COVID-19 test at least once a week and wear a mask while in the workplace. On November 4, 2021, it was announced that the mask mandate deadline is December 5, 2021 and by January 4, 2022 companies must require their workers to be fully vaccinated or submit to weekly coronavirus testing. It is unclear, among other things, how compliance will be documented and enforced but could include investigating complaints through OSHA's whistle-blower system and penalties. As a company with more than 100 employees, we will be required to mandate COVID-19 vaccination of our workforce or have our unvaccinated employees undergo required weekly COVID-19 testing.

In addition, rules were adopted requiring all federal employees to be fully vaccinated by November 22, 2021. Further, federal agencies are expected to require vaccinations for any employees or other personnel working under an agreement with an agency not covered by the mandate. This is expected to apply to federal contractors and subcontractors, such as us.

Any requirement to mandate COVID-19 vaccination of our workforce or require our unvaccinated employees to be tested weekly could result in employee attrition and difficulty securing future labor needs, and may have an adverse effect on our future revenues, costs and results of operations.

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

The Company may repurchase AAON, Inc. stock on the open market from time to time, up to a total of 5.7 million shares. We have repurchased a total of approximately 4.2 million shares (at current market prices) under the various open market stock buyback programs for an aggregate price of $74.8 million, or an average price of $17.79 per share. The Board must authorize the timing and amount of these purchases and all repurchases are in accordance with the rules and regulations of the SEC allowing the Company to repurchase shares from the open market.

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, Inc. stock in their accounts sold to the Company. The maximum number of shares to be repurchased is contingent upon the number of shares sold by employees. From inception through September 30, 2021, we repurchased approximately 8.1 million shares (at current market prices) for an aggregate price of $160.0 million, or an average price of $19.69 per share.

Lastly, the Company repurchases shares of AAON, Inc. stock from certain of its directors and employees for payment of statutory tax withholdings on stock transactions. All other repurchases from directors or employees are contingent upon Board approval. All repurchases are done at current market prices. From inception through September 30, 2021, we repurchased approximately 2.0 million shares (at current market prices) for an aggregate price of $22.3 million, or an average price of $11.00 per share.

Repurchases during the third quarter of 2021 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 2021	20,483	$ 61.73	20,483	—
August 2021	28,388	68.11	28,388	—
September 2021	23,221	66.75	23,221	—
Total	72,092	$ 65.86	72,092	—

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

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

None.

Item 5. Other Information.

None.

Item 6. Exhibits.

Exhibit #	Description
31.1	Certification by Chief Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by Chief Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by Chief Executive Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification by Chief Financial Officer furnished pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	Interactive data files pursuant to Rule 405 of Regulation S-T formatted in iXBRL (Inline Extensible Business Reporting Language): (i) our Consolidated Balance Sheets as of September 30, 2021 and December 31, 2020; (ii) our Consolidated Statements of Income for the three and nine months ended September 30, 2021 and 2020; (iii) our Consolidated Statements of Stockholders' Equity for the three and nine months ended September 30, 2021 and 2020; (iv) our Consolidated Statements of Cash Flows for the nine months ended September 30, 2021 and 2020; and (vi) the notes to our Consolidated Financial Statements.
104	Cover Page Interactive Data File pursuant to Rule 406 of Regulation S-T formatted in iXBRL (Inline Extensible Business Reporting Language) and contained in Exhibit 101.

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 4, 2021	By:	/s/ Gary D. Fields Gary D. Fields Chief Executive Officer
Dated: November 4, 2021	By:	/s/ Rebecca A. Thompson Rebecca A. Thompson Chief Financial Officer

Exhibit 31.1

CERTIFICATION

I, Gary D. Fields, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of AAON, Inc.

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

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

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

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

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles; and

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

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

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

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

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

Date: November 4, 2021

/s/ Gary D. Fields

Gary D. Fields
Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, Rebecca A. Thompson, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of AAON, Inc.

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

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

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

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

   b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles; and

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

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

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

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

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

Date: November 4, 2021

/s/ Rebecca A. Thompson

Rebecca A. Thompson
Chief Financial Officer

Exhibit 32.1

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

In connection with the Quarterly Report of AAON, Inc. (the “Company”), on Form 10-Q for the quarter ended September 30, 2021, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Gary D. Fields, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

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

Date: November 4, 2021

/s/ Gary D. Fields

Gary D. Fields
Chief Executive Officer

Exhibit 32.2

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

In connection with the Quarterly Report of AAON, Inc. (the “Company”), on Form 10-Q for the quarter ended September 30, 2021, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Rebecca A. Thompson, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

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

Date: November 4, 2021

/s/ Rebecca A. Thompson

Rebecca A. Thompson
Chief Financial Officer