

**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 March 31, 2022

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) | |
| <u>(918) 583-2266</u> | |
| (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 | <input checked="" type="checkbox"/> Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> Smaller reporting company | <input checked="" type="checkbox"/> |
| | Emerging growth company | <input type="checkbox"/> |

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 May 2, 2022, registrant had outstanding a total of 53,071,178 shares of its \$.004 par value Common Stock.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

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

| | <u>March 31, 2022</u> | <u>December 31, 2021</u> |
|---|-----------------------|--------------------------|
| Assets | | |
| <i>(in thousands, except share and per share data)</i> | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 5,633 | \$ 2,859 |
| Restricted cash | 595 | 628 |
| Accounts receivable, net of allowance for credit losses of \$837 and \$549, respectively | 113,736 | 70,780 |
| Income tax receivable | 2,092 | 5,723 |
| Inventories, net | 146,091 | 130,270 |
| Contract assets | 10,001 | 5,749 |
| Prepaid expenses and other | 5,548 | 2,071 |
| Total current assets | 283,696 | 218,080 |
| Property, plant and equipment: | | |
| Land | 5,016 | 5,016 |
| Buildings | 139,089 | 135,861 |
| Machinery and equipment | 326,306 | 318,259 |
| Furniture and fixtures | 23,817 | 23,072 |
| Total property, plant and equipment | 494,228 | 482,208 |
| Less: Accumulated depreciation | 227,858 | 224,146 |
| Property, plant and equipment, net | 266,370 | 258,062 |
| Intangible assets, net | 67,310 | 70,121 |
| Goodwill | 81,892 | 85,727 |
| Right of use assets | 16,862 | 16,974 |
| Other long-term assets | 1,328 | 1,216 |
| Total assets | \$ 717,458 | \$ 650,180 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 35,796 | \$ 29,020 |
| Accrued liabilities | 52,890 | 50,206 |
| Contract liabilities | 25,540 | 7,542 |
| Total current liabilities | 114,226 | 86,768 |
| Revolving credit facility, long-term | 65,000 | 40,000 |
| Deferred tax liabilities | 32,966 | 31,993 |
| Other long-term liabilities | 18,693 | 18,843 |
| New market tax credit obligation (a) | 6,417 | 6,406 |
| 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, 53,065,081 and 52,527,985 issued and outstanding at March 31, 2022 and December 31, 2021, respectively | 212 | 210 |
| Additional paid-in capital | 77,574 | 81,654 |
| Retained earnings | 402,370 | 384,306 |
| Total stockholders' equity | 480,156 | 466,170 |
| Total liabilities and stockholders' equity | \$ 717,458 | \$ 650,180 |
| (a) Held by variable interest entities (Note 17) | | |

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

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

| | Three Months Ended March 31, | |
|--|--|-------------------|
| | 2022 | 2021 |
| | <i>(in thousands, except share and per share data)</i> | |
| Net sales | \$ 182,771 | \$ 115,788 |
| Cost of sales | 136,707 | 82,631 |
| Gross profit | 46,064 | 33,157 |
| Selling, general and administrative expenses | 23,056 | 14,696 |
| Gain on disposal of assets | (2) | — |
| Income from operations | 23,010 | 18,461 |
| Interest (expense) income, net | (190) | 3 |
| Other income, net | 21 | 17 |
| Income before taxes | 22,841 | 18,481 |
| Income tax provision | 4,782 | 2,105 |
| Net income | <u>\$ 18,059</u> | <u>\$ 16,376</u> |
| Earnings per share: | | |
| Basic | <u>\$ 0.34</u> | <u>\$ 0.31</u> |
| Diluted | <u>\$ 0.33</u> | <u>\$ 0.30</u> |
| Weighted average shares outstanding: | | |
| Basic | <u>52,613,232</u> | <u>52,293,464</u> |
| Diluted | <u>53,950,995</u> | <u>53,814,644</u> |

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

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

| | Three Months Ended March 31, 2022 | | | | |
|--|--|----------------|------------------|-------------------|-------------------|
| | Common Stock | Paid-in | | Retained | Total |
| | Shares | Amount | Capital | Earnings | |
| | <i>(in thousands)</i> | | | | |
| Balances at December 31, 2021 | 52,528 | \$ 210 | \$ 81,654 | \$ 384,306 | \$ 466,170 |
| Net income | — | — | — | 18,059 | 18,059 |
| Stock options exercised, restricted stock awards granted, and contingent shares issued (Note 16) | 605 | 2 | 2,890 | — | 2,892 |
| Share-based compensation | — | — | 3,112 | — | 3,112 |
| Stock repurchased and retired | (68) | — | (4,082) | — | (4,082) |
| Contingent consideration (Note 3) | — | — | (6,000) | — | (6,000) |
| Refund for cancelled cash dividends | — | — | — | 5 | 5 |
| Balances at March 31, 2022 | <u>53,065</u> | <u>\$ 212</u> | <u>\$ 77,574</u> | <u>\$ 402,370</u> | <u>\$ 480,156</u> |

| | Three Months Ended March 31, 2021 | | | | |
|---|--|----------------|------------------|-------------------|-------------------|
| | Common Stock | Paid-in | | Retained | Total |
| | Shares | Amount | Capital | Earnings | |
| | <i>(in thousands)</i> | | | | |
| Balances at December 31, 2020 | 52,225 | \$ 209 | \$ 5,161 | \$ 345,495 | 350,865 |
| Net income | — | — | — | 16,376 | 16,376 |
| Stock options exercised and restricted stock awards granted | 286 | 2 | 9,436 | — | 9,438 |
| Share-based compensation | — | — | 2,761 | — | 2,761 |
| Stock repurchased and retired | (87) | (1) | (6,401) | — | (6,402) |
| Balances at March 31, 2021 | <u>52,424</u> | <u>\$ 210</u> | <u>\$ 10,957</u> | <u>\$ 361,871</u> | <u>\$ 373,038</u> |

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

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

| | Three Months Ended | |
|---|---------------------------|------------------|
| | March 31, | |
| | 2022 | 2021 |
| Operating Activities | <i>(in thousands)</i> | |
| Net income | \$ 18,059 | \$ 16,376 |
| Adjustments to reconcile net income to net cash (used in) provided by operating activities: | | |
| Depreciation and amortization | 7,076 | 7,398 |
| Amortization of debt issuance cost | 11 | 10 |
| Amortization of right of use assets | 67 | — |
| Provision for (recovery of) credit losses on accounts receivable, net of adjustments | 288 | (13) |
| Provision for (recovery of) excess and obsolete inventories | 220 | (194) |
| Share-based compensation | 3,112 | 2,761 |
| Gain on disposition of assets | (2) | — |
| Foreign currency transaction gain | (9) | (8) |
| Interest income on note receivable | (6) | (6) |
| Deferred income taxes | 973 | 4,658 |
| Changes in assets and liabilities: | | |
| Accounts receivable | (43,244) | (5,179) |
| Income tax receivable | 3,631 | (2,766) |
| Inventories | (16,041) | (1,627) |
| Contract assets | (4,252) | — |
| Prepaid expenses and other | (3,588) | 108 |
| Accounts payable | 6,325 | 4,904 |
| Contract liabilities | 17,998 | — |
| Deferred revenue | 68 | 2,358 |
| Accrued liabilities | 2,511 | 58 |
| Net cash (used in) provided by operating activities | <u>(6,803)</u> | <u>28,838</u> |
| Investing Activities | | |
| Capital expenditures | (14,031) | (16,404) |
| Cash paid in business combination, net of cash acquired | (249) | — |
| Proceeds from sale of property, plant and equipment | 2 | — |
| Principal payments from note receivable | 14 | 14 |
| Net cash used in investing activities | <u>(14,264)</u> | <u>(16,390)</u> |
| Financing Activities | | |
| Borrowings under revolving credit facility | 25,000 | — |
| Stock options exercised | 2,890 | 9,438 |
| Repurchase of stock | (3,278) | (5,185) |
| Employee taxes paid by withholding shares | (804) | (1,217) |
| Net cash provided by financing activities | <u>23,808</u> | <u>3,036</u> |
| Net increase in cash, cash equivalents and restricted cash | <u>2,741</u> | <u>15,484</u> |
| Cash, cash equivalents and restricted cash, beginning of period | <u>3,487</u> | <u>82,288</u> |
| Cash, cash equivalents and restricted cash, end of period | <u>\$ 6,228</u> | <u>\$ 97,772</u> |

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

AAON, Inc. is a Nevada corporation which was incorporated on August 18, 1987. Our operating subsidiaries include AAON, Inc., an Oklahoma corporation, AAON Coil Products, Inc., a Texas corporation, and BasX, Inc. (dba BasX Solutions), an Oregon corporation (collectively, the "Company"). The accompanying unaudited consolidated financial statements of AAON, Inc. and our operating subsidiaries, all of which are wholly-owned, 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").

On December 10, 2021, we closed on the acquisition of all of the issued and outstanding equity ownership of BasX, LLC, doing business as BasX Solutions ("BasX") (Note 3). We began including the results of BasX's operations in our consolidated financial statements on December 11, 2021. On December 29, 2021, BasX, LLC converted to a C-Corporation, BasX, Inc., and is subject to income tax.

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 17) 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, 2021 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, 2021. All intercompany balances and transactions have been eliminated in consolidation.

We are engaged in the engineering, manufacturing, marketing, and sale of premium air conditioning and heating equipment consisting of standard, semi-custom, and custom rooftop units, data centers cooling solutions, cleanroom systems, 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, useful lives of property, plant, and equipment, and share-based compensation. Actual results could differ materially from those estimates.

Change in Estimate

During the first quarter of 2022, a review of the Company's useful lives for certain sheet metal manufacturing equipment at our Longview, Texas location resulted in a change in estimate that increased the useful lives from between ten and twelve years to fifteen years. This determination was based on recent and estimated future production levels as well as management's knowledge of the equipment and historical and future use of the equipment. The change in estimate was made prospectively and resulted in a decrease to depreciation expense within cost of sales on our consolidated statements of income of \$1.8 million during the three months ended March 31, 2022.

Impact of COVID-19 Pandemic

The magnitude of the impact of COVID-19 remains unpredictable and we, therefore, continue to anticipate potential supply chain disruptions, employee absenteeism, and additional health and safety costs related to the COVID-19 pandemic that could unfavorably impact our business.

We had continuous operations during the three months ended March 31, 2022. 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 also utilizes sanitation stations and performs additional cleaning and sanitation throughout the day.

Although future disruptions and costs are expected to be temporary, there is significant uncertainty around the duration and overall impact to our business operations. We are continually monitoring the progression of the pandemic, including new COVID-19 variants, and its potential effect on our financial position, results of operations and cash flows.

Inflation and Labor Market

We have witnessed increases of our raw material prices, especially in copper and steel, which appear to be a residual effect of COVID-19, and we continue to make strategic purchases of materials when we see opportunities. We have managed the increase in the cost of raw materials through price increases for our products. We have also experienced supply chain challenges related to specific manufacturing parts, which we have managed through our strong existing vendor relationships, expanding our list of vendors, and our favorable liquidity position.

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 put a cost of living increase of 3.5% in place in October 2021 for all employees below the Director level. In March 2022, we awarded annual merit raises resulting in a 3.0% increase in overall wages. We will continue to implement human resource initiatives to retain and attract labor to further improve productivity and production efficiencies.

Despite efforts to mitigate the impact of inflation, supply chain issues, and the tight labor market, future disruptions, while temporary, could negatively impact our financial position, results of operations and cash flows.

First Quarter 2021 Planned Maintenance and Adverse Weather

During the fourth quarter of 2020, we made the strategic decision to shut down our Tulsa, OK and Longview, TX manufacturing facilities to perform planned and necessary maintenance during the last week of December 2020 as well several days in early January 2021.

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.

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, 2021.

Fair Value Measurements

The carrying amounts of cash and cash equivalents, receivables, accounts payable, and accrued liabilities approximate fair value because of the short-term maturity of the items. The carrying amount of the Company's revolving line of credit, and other payables, approximate their fair values either due to their short term nature, the variable rates associated with the debt, or based on current rates offered to the Company for debt with similar characteristics.

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, contingent consideration, 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.

Definite-Lived Intangible Assets

Our definite-lived intangible assets include various trademarks, service marks, and technical knowledge acquired in business combinations (Note 3). We evaluate the carrying value of our amortizable intangible assets for potential impairment when events and circumstances warrant such a review.

Amortization is computed using the straight-line method over the following estimated useful lives:

| | |
|------------------------|----------|
| Intellectual property | 30 years |
| Customer relationships | 14 years |

Goodwill and Indefinite-Lived Intangible Assets

Goodwill represents the excess of the consideration paid for the acquired businesses over the fair value of the individual assets acquired, net of liabilities assumed. At March 31, 2022 \$50.3 million of goodwill is deductible for income tax purposes. Our indefinite-lived intangible assets consist of trademark and trade names. Goodwill and indefinite-lived intangible assets are not amortized, but instead are 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.

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 not listed or included within the Company's Annual Report on Form 10-K for the year ended December 31, 2021, 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

The following tables show disaggregated net sales by reportable segment (see Note 20) by major source, net of intercompany sales eliminations. As the BasX segment was not applicable during the three months ended March 31, 2021, this segment has been excluded from the table for that period.

| | Three Months Ended March 31, 2022 | | | |
|-------------------------------|-----------------------------------|-----------------------|-------------------|-------------------|
| | AAON Oklahoma | AAON Coil Products | BasX | Total |
| | <i>(in thousands)</i> | | | |
| Rooftop Units | \$ 121,706 | \$ — | \$ — | \$ 121,706 |
| Condensing Units | 242 | 8,976 | — | 9,218 |
| Air Handlers | — | 9,438 | 1,339 | 10,777 |
| Outdoor Mechanical Rooms | 554 | 110 | — | 664 |
| Cleanroom Systems | — | — | 8,039 | 8,039 |
| Data Center Cooling Solutions | — | — | 10,868 | 10,868 |
| Water-Source Heat Pumps | 2,986 | 2,353 | — | 5,339 |
| Part Sales | 10,216 | — | — | 10,216 |
| Other ² | 4,163 | 1,058 | 723 | 5,944 |
| | <u>\$ 139,867</u> | <u>\$ 21,935</u> | <u>\$ 20,969</u> | <u>\$ 182,771</u> |
| | Three Months Ended March 31, 2021 | | | |
| | AAON Oklahoma | AAON Coil Products | BasX ¹ | Total |
| | <i>(in thousands)</i> | | | |
| Rooftop Units | \$ 87,425 | \$ — | — | \$ 87,425 |
| Condensing Units | 249 | 6,282 | — | 6,531 |
| Air Handlers | — | 6,414 | — | 6,414 |
| Outdoor Mechanical Rooms | 63 | 148 | — | 211 |
| Water-Source Heat Pumps | 2,388 | 2,277 | — | 4,665 |
| Part Sales | 7,506 | — | — | 7,506 |
| Other ² | 2,345 | 691 | — | 3,036 |
| | <u>\$ 99,976</u> | <u>\$ 15,812</u> | <u>—</u> | <u>\$ 115,788</u> |

¹ BasX was acquired by the Company on December 10, 2021.

² Other sales include freight, extended warranties and miscellaneous revenue.

Due to the highly customized nature of many of the Company's products and each product not having an alternative use to the Company without significant costs to the Company, the Company recognizes revenue over time as progress is made toward satisfying the performance obligations of each contract. The Company has formal cancellation policies 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. The Company measures a contract's progress on

the basis of the ratio that costs incurred bear to estimated total costs using the input method because, in the Company's view, such method best depicts the progress toward completion.

Contract costs include direct materials, direct labor, installation, freight and delivery, commissions and royalties. Other costs not related to contract performance, such as indirect labor and materials, small tools and supplies, operating expenses, field rework and back charges are charged to expense as incurred. Provisions for estimated losses on contracts in progress are made in the period in which such losses are determined. Changes in job performance, job conditions, and estimated profitability, including those arising from contract penalty provisions and final contract settlements, may result in revisions to costs and income, and are estimated and recognized by the Company throughout the life of the contract. The aggregate of costs incurred and income recognized on uncompleted contracts in excess of billings is shown as a contract asset within our consolidated balance sheets, and the aggregate of billings on uncompleted contracts in excess of related costs incurred and income recognized is shown as a contract liability within our consolidated balance sheets.

For all other products that are part sales or standardized units, the Company recognizes revenue, presented net of sales tax, when it satisfies the performance obligation in its contracts. As the primary performance obligation in such a contract is delivery of the requested manufactured equipment, 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.

Product Warranties

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.

Representatives and Third Party Products

We are responsible for billings and collections resulting from all sales transactions, including those initiated by our independent manufacturer representatives ("Representatives"). Representatives are national companies that are in the business of providing HVAC units and other related products and services to customers. The end user customer orders a bundled group of products and services from the Representative and expects the Representative to fulfill the order. These additional products and services may include controls purchased from another manufacturer to operate the unit, start-up services, and curbs for supporting the unit ("Third Party Products"). All are associated with the purchase of a HVAC unit but may be provided by the Representative or another third party. 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 \$6.5 million and \$11.0 million for the three months ended March 31, 2022 and 2021, respectively.

3. Business Combination

On November 18, 2021, the Company entered into a membership interest purchase agreement (the "MIPA Agreement") to acquire all of the issued and outstanding equity ownership of BasX, LLC, an Oregon limited liability company, doing business as BasX Solutions. We closed this transaction on December 10, 2021 for a purchase price of (i) \$100.0 million payable in cash (not including working capital adjustments), and (ii) up to \$80.0 million in the aggregate of contingent consideration payable in shares of the Company's stock, par value \$0.004 per share (the "Shares").

The \$80.0 million of contingent consideration payable consists of \$78.0 million payable to the former owners of BasX and \$2.0 million payable to key employees of BasX whom are now employed by the Company. The potential future issuance of the Shares is contingent upon BasX meeting certain post-closing earn-out milestones during each of 2021, 2022, and 2023 under the terms of the MIPA Agreement. The Company funded the BasX acquisition cash portion of the purchase price and related transaction costs with cash on hand.

Additionally, as a condition to closing, the Company entered into a real estate purchase agreement with BasX Properties, LLC, an affiliate of BasX, to acquire the principal real property and improvements utilized by BasX for an additional \$22.0 million, subject to customary closing conditions and adjustments. The Company expects this real estate transaction to close by the end of the second quarter of 2022.

BasX specializes in the design, engineering and manufacturing of custom, energy efficient cooling solutions for the rapidly growing hyperscale data center market. BasX also designs and manufactures custom solutions for cleanroom environments for the bio-pharmaceutical, semiconductor, medical and agriculture markets, as well as custom, energy efficient air handlers and modular solutions for a vast array of markets. The acquisition of BasX brings the Company exposure to attractive end-markets into which the Company has historically had minimal exposure. The products BasX manufactures are highly engineered, customized products, fully complimenting AAON's existing business.

We applied pushdown accounting, allowable under ASC 805 "Business Combinations," to "pushdown" our stepped-up basis in the assets acquired and liabilities assumed to BasX's subsidiary financial statements. The decision to apply pushdown accounting is irrevocable. Goodwill was calculated and recognized consistent with acquisition accounting, resulting in the pushdown of \$78.7 million in goodwill.

The following table presents the revised allocation of the consideration paid to the assets acquired and liabilities assumed in the acquisition of BasX described above, which was still preliminary at December 31, 2021. The revisions indicated below were recorded during the three months ended March 31, 2022. The revisions were the results of updates to our preliminary estimates and third party valuation models. The impact of such revisions on net income for prior periods was not significant.

| | Revised Allocation as of March 31, 2022 | Estimated Allocation as of December 31, 2021 | Revision |
|---|--|---|-----------------|
| | <i>(in thousands)</i> | | |
| Accounts receivable | \$ 13,699 | \$ 13,699 | \$ — |
| Inventories | 2,725 | 2,725 | — |
| Contract assets | 7,635 | 7,635 | — |
| Prepaid expenses and other | 341 | 341 | — |
| Property, plant and equipment | 13,169 | 13,169 | — |
| Right of use assets | 15,611 | 15,611 | — |
| Intangible assets | 68,413 | 70,329 | (1,916) |
| Goodwill | 78,663 | 82,498 | (3,835) |
| Accounts payable | (9,388) | (9,388) | — |
| Accrued liabilities | (3,807) | (3,807) | — |
| Contract liabilities | (7,771) | (7,771) | — |
| Lease liabilities | (15,611) | (15,611) | — |
| Contingent Consideration - shares of AAON, Inc. | (60,000) | (66,000) | 6,000 |
| Consideration paid | <u>\$ 103,679</u> | <u>\$ 103,430</u> | <u>\$ 249</u> |

The Company recognized the following definite and indefinite-lived intangible assets as part of the acquisition of BasX:

| | Revised Allocation as of March 31, 2022 | Estimated Allocation as of December 31, 2021 | Revision |
|---|--|---|--------------------------|
| <i>(in thousands)</i> | | | |
| Definite-lived intangible assets | | | |
| Intellectual property | \$ 6,295 | \$ 6,479 | \$ (184) |
| Customer relationships | 47,547 | 48,684 | (1,137) |
| | <u>53,842</u> | <u>55,163</u> | <u>(1,321)</u> |
| Indefinite-lived intangible assets | | | |
| Trademarks | 14,571 | 15,166 | (595) |
| Total intangible assets acquired | <u>\$ 68,413</u> | <u>\$ 70,329</u> | <u>\$ (1,916)</u> |

Goodwill is the excess of the consideration paid for the acquired businesses over the fair value of the individual assets acquired, net of liabilities assumed. Goodwill represents a premium paid to acquire the skilled workforce and expanded market opportunities. Goodwill of \$47.1 million is tax deductible upon close of the acquisition. Future additional amounts of goodwill related to the contingent consideration may become tax deductible in the future if the earn out provisions of the MIPA Agreement are achieved.

Pro Forma Results of Operations (unaudited)

The operations of BasX have been included in our statements of income since the closing date on December 10, 2021. The following unaudited pro forma consolidated results of operations for the three months ended March 31, 2021 are presented as if the combination had been made on January 1, 2021.

| | <i>(unaudited)</i> | |
|---------------------|--|---------|
| | Three months ended | |
| | March 31, 2021 | |
| | <i>(in thousands, except per share data)</i> | |
| Revenues | \$ | 130,631 |
| Net income | | 16,972 |
| Earnings per share: | | |
| Basic | \$ | 0.32 |
| Dilutive | \$ | 0.32 |

These unaudited pro forma results include adjustments necessary in connection with the acquisition.

The unaudited consolidated pro forma financial information was prepared in accordance with GAAP and is not necessarily indicative of the results of operations that would have occurred if the acquisition had been completed on the date indicated, nor is it indicative of the future operating results of the Company.

The unaudited pro forma results do not reflect events that either have occurred or may occur after the acquisition date, including, but not limited to, the anticipated realization of operating synergies in subsequent periods. These results also do not give effect to certain charges that the Company expects to incur in connection with the acquisition, including, but not limited to, additional professional fees and employee integration.

4. Leases

All of our leases are classified as operating leases. As our leases do not provide an implicit interest rate, we use our incremental borrowing rate based on the information available at the commencement date in determining the present value of lease

payments. Our incremental borrowing rate represents the interest rate which we would pay to borrow, on a collateralized basis, an amount equal to the lease payments over a similar term in a similar economic environment.

We have entered into various short-term operating leases with an initial term of twelve months or less. We have elected the short-term lease measurement and recognition exemption which does not require balance sheet presentation these short-term leases. The rent expense for these short-term leases is not significant.

The Company's leases generally require us to pay for insurance, taxes, utilities, and other operating costs. These payments are not included in the right-of-use asset or lease liability and are expensed as incurred.

Through the acquisition of BasX (Note 3), we acquired various leases for plant/office space and equipment. We also lease the plant/office space used by our operations in Parkville, MO. Expense related to these leases is recognized on straight-line basis over the lease term. Certain of our leases contain escalating lease payments based on predefined increases. Most leases contain options to renew or terminate. Right-of-use assets and lease liabilities reflect only the options which the Company is reasonably certain to exercise.

At March 31, 2022, we had operating lease right-of-use assets of \$16.9 million, current and noncurrent operating lease obligations of \$1.7 million and \$15.3 million within accrued liabilities and other long-term liabilities, respectively, on our consolidated balance sheets. At December 31, 2021, we had operating lease right-of-use assets of \$17.0 million and current and noncurrent operating lease obligations of \$1.6 million and \$15.5 million within accrued liabilities and other long-term liabilities, respectively, on our consolidated balance sheets.

5. Accounts Receivable

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

| | March 31, 2022 | December 31, 2021 |
|---|---------------------------|------------------------------|
| | <i>(in thousands)</i> | |
| Accounts receivable | \$ 114,573 | \$ 71,329 |
| Less: Allowance for credit losses | (837) | (549) |
| Total, net | <u>\$ 113,736</u> | <u>\$ 70,780</u> |
| | Three Months Ended | |
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Allowance for credit losses: | | |
| Balance, beginning of period | \$ 549 | \$ 506 |
| Provisions for (recoveries of) expected credit losses, net of adjustments | 288 | (13) |
| Balance, end of period | <u>\$ 837</u> | <u>\$ 493</u> |

6. 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:

| | March 31, 2022 | December 31, 2021 |
|---|---------------------------|------------------------------|
| | <i>(in thousands)</i> | |
| Raw materials | \$ 140,424 | \$ 124,480 |
| Work in process | 3,003 | 3,049 |
| Finished goods | 4,671 | 4,528 |
| Total, gross | 148,098 | 132,057 |
| Less: Allowance for excess and obsolete inventories | (2,007) | (1,787) |
| Total, net | <u>\$ 146,091</u> | <u>\$ 130,270</u> |

| | Three Months Ended | |
|--|---------------------------|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Allowance for excess and obsolete inventories: | | |
| Balance, beginning of period | \$ 1,787 | \$ 3,261 |
| Provision for (recovery of) excess and obsolete inventories | 220 | (194) |
| Inventories written off | — | (763) |
| Balance, end of period | <u>\$ 2,007</u> | <u>\$ 2,304</u> |

7. Intangible assets

Our intangible assets consist of the following:

| | <u>March 31, 2022</u> | <u>December 31, 2021</u> |
|------------------------------------|-----------------------|--------------------------|
| Definite-lived intangible assets | <i>(in thousands)</i> | |
| Intellectual property | \$ 6,295 | \$ 6,479 |
| Customer relationships | 47,547 | 48,684 |
| Less: Accumulated amortization | (1,103) | (208) |
| Total, net | <u>52,739</u> | <u>54,955</u> |
| Indefinite-lived intangible assets | | |
| Trademarks | 14,571 | 15,166 |
| Total intangible assets, net | <u>\$ 67,310</u> | <u>\$ 70,121</u> |

Amortization expense recorded in cost of sales is as follows:

| | Three Months Ended | |
|----------------------|---------------------------|---------------------------|
| | <u>March 31, 2022</u> | <u>March 31, 2021</u> |
| | <i>(in thousands)</i> | |
| Amortization expense | \$ 895 | \$ 38 |

Excluding the impact of any future acquisitions, the Company anticipates amortization expense to be \$3.6 million for each of the years ended 2022 through 2026.

8. Supplemental Cash Flow Information

| | Three Months Ended | |
|--|---------------------------|---------------------------|
| | <u>March 31, 2022</u> | <u>March 31, 2021</u> |
| Supplemental disclosures: | <i>(in thousands)</i> | |
| Interest paid | \$ 115 | \$ — |
| Income taxes paid | \$ 176 | \$ 213 |
| Non-cash investing and financing activities: | | |
| Non-cash capital expenditures | \$ 458 | \$ 264 |

9. Warranties

The Company has product warranties with various terms ranging from one year from the date of first use or 18 months for parts, data center cooling solutions, and cleanroom systems 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 | |
|------------------------------|---------------------------|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| Warranty accrual: | <i>(in thousands)</i> | |
| Balance, beginning of period | \$ 13,769 | \$ 13,522 |
| Payments made | (1,219) | (1,464) |
| Provisions | 1,157 | 1,467 |
| Balance, end of period | <u>\$ 13,707</u> | <u>\$ 13,525</u> |
| Warranty expense: | \$ 1,157 | \$ 1,467 |

10. Accrued Liabilities and Other Long-Term Liabilities

Accrued liabilities were comprised of the following:

| | March 31, 2022 | December 31, 2021 |
|---------------------------------------|---------------------------|------------------------------|
| | <i>(in thousands)</i> | |
| Warranty | \$ 13,707 | \$ 13,769 |
| Due to representatives | 13,453 | 7,995 |
| Payroll | 7,601 | 8,423 |
| Profit sharing | 2,670 | 1,489 |
| Worker's compensation | 261 | 308 |
| Medical self-insurance | 1,208 | 1,943 |
| Customer prepayments | 2,870 | 5,931 |
| Donations | 453 | 438 |
| Employee vacation time | 5,000 | 4,362 |
| Operating lease liability, short-term | 1,683 | 1,580 |
| Other | 3,984 | 3,968 |
| Total | <u>\$ 52,890</u> | <u>\$ 50,206</u> |

Other long-term liabilities were comprised of the following:

| | March 31, 2022 | December 31, 2021 |
|--------------------------------------|---------------------------|------------------------------|
| | <i>(in thousands)</i> | |
| Long-term operating lease obligation | \$ 15,320 | \$ 15,467 |
| Long-term donations | 221 | 334 |
| Extended warranties | 3,152 | 3,042 |
| Total | <u>\$ 18,693</u> | <u>\$ 18,843</u> |

11. Revolving Credit Facility

On November 24, 2021, we amended our revolving credit facility ("Revolver"), to provide for maximum borrowings of \$100.0 million, with an option to increase to maximum borrowing of \$200.0 million. As of March 31, 2022 and December 31, 2021, we had \$65.0 million and \$40.0 million outstanding under the Revolver, respectively. We have one standby letter of credit totaling \$0.8 million as of March 31, 2022. Borrowings available under the Revolver at March 31, 2022 were \$34.2 million. The Revolver expires on November 24, 2026.

Any outstanding loans under the Revolver bear interest at the daily compounded secured overnight financing rate ("SOFR") plus the applicable margin. Applicable margin, ranging from 1.25% - 1.75%, is determined quarterly based on the Company's leverage ratio. The Company is also subject to letter of credit fees, ranging from 1.25% - 1.75%, and a commitment fee, ranging from 0.10% - 0.20%. The applicable fee percentage is determined quarterly based on the Company's leverage ratio. As of and for the three months ended March 31, 2022, the weighted average interest rate of our the Revolver was 1.3%. Fees associated with the unused portion of the committed amount are included in interest expense on our consolidated statements of income and were not material for the three months ended March 31, 2022.

If SOFR cannot be determined pursuant to the definition, as defined by the Revolver agreement, any outstanding effected loans will be deemed to have been converted into alternative base rate ("ABR") loans. ABR loans would bear interest at a rate per annum equal to the highest of (a) the Prime Rate in effect on such day, (b) the Federal Funds Rate in effect on such day plus 0.50%, or (c) daily simple SOFR for a one-month tenor in effect on such day plus 1.00%.

At March 31, 2022, we were in compliance with our financial covenants, as defined by the Revolver. These covenants require that we meet certain parameters related to our leverage ratio. At March 31, 2022, our leverage ratio was 0.63 to 1.0, which meets the requirement of not being above 3 to 1.

12. Income Taxes

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

| | Three Months Ended | |
|----------------------|-----------------------|-------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Current | \$ 3,809 | \$ (2,553) |
| Deferred | 973 | 4,658 |
| Income tax provision | <u>\$ 4,782</u> | <u>\$ 2,105</u> |

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 | |
|--|--------------------|-------------------|
| | March 31, 2022 | March 31, 2021 |
| Federal statutory rate | 21.0 % | 21.0 % |
| State income taxes, net of Federal benefit | 3.0 | 7.5 |
| Excess tax benefits | (2.2) | (15.8) |
| Return to provision adjustments | — | (0.4) |
| Other | (0.9) | (0.9) |
| Effective tax rate | <u>20.9 %</u> | <u>11.4 %</u> |

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%. This resulted in an overall reduction of our effective state income tax rate, net of Federal benefit.

During the three months ended March 31, 2022, the Company recorded an excess tax benefit of \$0.5 million as compared to \$2.9 million during the same period in 2021, a decrease of 82%. The decrease 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 March 31, 2022, we have investment tax credit carryforwards of approximately \$3.7 million. These credits have estimated expirations from the year 2036 through 2040.

The Company's estimated annual 2022 effective tax rate, excluding discrete events, is approximately 25%. We file income tax returns in the U.S., state and foreign income tax returns jurisdictions. We are subject to U.S. income tax examinations for tax years 2018 to present, and to non-U.S. income tax examinations for the tax years 2017 to present. In addition, we are subject to state and local income tax examinations for the tax years 2017 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.

13. 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 ("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 may delegate certain duties to one or more officers of the Company as provided in the 2016 Plan. The Committee determines the persons to whom awards are to be made, determines 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.

Options

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 three months ended March 31, 2022 and 2021 using a Black Scholes-Merton Model:

| | Three months ended | |
|---------------------------------------|--------------------|----------------|
| | March 31, 2022 | March 31, 2021 |
| Directors and SLT¹: | | |
| Expected dividend rate | \$0.38 | \$0.38 |
| Expected volatility | 35.87% | 35.78% |
| Risk-free interest rate | 2.11% | 0.50% |
| Expected life (in years) | 4.0 | 4.0 |
| Employees: | | |
| Expected dividend rate | \$0.38 | \$0.38 |
| Expected volatility | 37.16% | 38.70% |
| Risk-free interest rate | 1.98% | 0.30% |
| Expected life (in years) | 3.0 | 3.0 |

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 March 31, 2022:

| Range of Exercise Prices | Number of Shares | Weighted Average Remaining Contractual Life (in years) | Weighted Average Exercise Price | Intrinsic Value (in thousands) |
|--------------------------|------------------|--|---------------------------------|--------------------------------|
| \$ 8.17 - \$ 41.37 | 1,323,510 | 5.73 | \$ 36.12 | \$ 25,953 |
| \$ 42.42 - \$ 65.24 | 271,925 | 7.82 | 44.72 | 3,005 |
| \$ 65.29 - \$ 79.81 | 101,868 | 8.86 | 73.22 | — |
| Total | 1,697,303 | 6.25 | \$ 39.72 | \$ 28,958 |

The following is a summary of stock options vested and exercisable as of March 31, 2021:

| Range of Exercise Prices | Number of Shares | Weighted Average Remaining Contractual Life (in years) | Weighted Average Exercise Price | Intrinsic Value (in thousands) |
|--------------------------|------------------|--|---------------------------------|--------------------------------|
| \$ 7.18 - \$ 40.87 | 621,552 | 5.58 | \$ 30.01 | \$ 24,863 |
| \$ 41.37 - \$ 41.37 | 427,899 | 7.86 | 41.37 | 12,255 |
| \$ 41.78 - \$ 75.00 | 143,232 | 8.75 | 44.45 | 3,661 |
| Total | 1,192,683 | 6.78 | \$ 35.82 | \$ 40,779 |

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

| Stock Options | Shares | Weighted Average Exercise Price |
|----------------------------------|------------------|--|
| Outstanding at December 31, 2021 | 3,365,469 | \$ 42.88 |
| Granted | 353,723 | 54.52 |
| Exercised | (79,169) | 36.51 |
| Forfeited or Expired | (25,288) | 51.58 |
| Outstanding at March 31, 2022 | <u>3,614,735</u> | <u>\$ 44.10</u> |
| Exercisable at March 31, 2022 | <u>1,697,303</u> | <u>\$ 39.72</u> |

The total pre-tax compensation cost related to unvested stock options not yet recognized as of March 31, 2022 is \$19.7 million and is expected to be recognized over a weighted average period of approximately 2.3 years.

The total intrinsic value of options exercised during the three months ended March 31, 2022 and 2021 was \$1.9 million and \$10.7 million, respectively. The cash received from options exercised during the three months ended March 31, 2022 and 2021 was \$2.9 million and \$9.4 million, respectively. The impact of these cash receipts is included in financing activities in the accompanying consolidated statements of cash flows.

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 March 31, 2022, unrecognized compensation cost related to unvested restricted stock awards was approximately \$5.8 million, which is expected to be recognized over a weighted average period of approximately 2.2 years.

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

| | Shares | Weighted Average Grant Date Fair Value |
|-------------------------------|----------------|---|
| Unvested at December 31, 2021 | 161,225 | \$ 46.08 |
| Granted | 39,903 | 53.55 |
| Vested | (48,479) | 42.20 |
| Forfeited | (581) | 49.75 |
| Unvested at March 31, 2022 | <u>152,068</u> | <u>\$ 49.26</u> |

PSUs

We have awarded performance restricted stock units ("PSUs") to certain officers and 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 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 three years. 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 March 31, 2022 is \$2.6 million and is expected to be recognized over a weighted average period of approximately 2.7 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 three months ended March 31, 2022 and 2021 using a Monte Carlo Model:

| | Three months ended | |
|--------------------------|---------------------------|-----------------------|
| | March 31, 2022 | March 31, 2021 |
| Expected dividend rate | \$0.38 | \$0.38 |
| Expected volatility | 37.60% | 39.10% |
| Risk-free interest rate | 2.00% | 0.28% |
| Expected life (in years) | 2.80 | 2.81 |

The expected term of the PSUs is based on their remaining performance period. 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, 2021 | 16,851 | \$ 87.78 |
| Granted | 41,621 | 44.74 |
| Vested | — | — |
| Forfeited | — | — |
| Unvested at March 31, 2022 | <u>58,472</u> | <u>\$ 57.14</u> |

Key Employee Awards

Subject to the MIPA Agreement (Note 3), the Company granted awards to key employees of BasX ("Key Employee Awards"). Unlike our restricted stock awards under the 2016 Plan, the Key Employee Awards are not considered legally outstanding and do not accrue dividends during the vesting period. The potential future issuance of the Key Employee Awards is contingent upon BasX meeting certain post-closing earn-out milestones during each of the years ending 2021, 2022 and 2023 as defined by the MIPA Agreement and continued employment with the Company. At the end of the earn-out period, ending December 31, 2023, each eligible Key Employee Award will vest and be converted into common stock. The fair value of Key Employee Awards is based on the fair market value of AAON common stock on the grant date. The Key Employee Awards do not accrue dividends.

The total pre-tax compensation cost related to unvested Key Employee Awards not yet recognized as of March 31, 2022 is \$1.5 million and is expected to be recognized over a weighted average period of approximately 1.8 years.

A summary of the unvested Key Employee Awards is as follows:

| | Shares | Weighted Average Grant Date Fair Value |
|-------------------------------|---------------|---|
| Unvested at December 31, 2021 | 26,599 | \$ 80.18 |
| Granted | — | — |
| Vested | — | — |
| Forfeited | — | — |
| Unvested at March 31, 2022 | <u>26,599</u> | <u>\$ 80.18</u> |

Share-Based Compensation

A summary of share-based compensation is as follows:

| | Three Months Ended | |
|---|---------------------------|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| Grant date fair value of awards during the period: | <i>(in thousands)</i> | |
| Options | \$ 4,849 | \$ 6,513 |
| Performance awards | 1,862 | 1,506 |
| Restricted stock | 2,137 | 1,400 |
| Total | \$ 8,848 | \$ 9,419 |
| Share-based compensation expense: | | |
| Options | \$ 2,040 | \$ 2,163 |
| Performance awards | 185 | 41 |
| Restricted stock | 679 | 557 |
| Key employee awards | 208 | — |
| Total | \$ 3,112 | \$ 2,761 |
| Income tax benefit/(deficiency) related to share-based compensation: | | |
| Options | \$ 293 | \$ 2,295 |
| Restricted stock | 219 | 615 |
| Total | \$ 512 | \$ 2,910 |

Share-based compensation expense is recognized on a straight-line basis over the service period of the related share-based compensation award. 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 share-based compensation 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. Forfeitures are accounted for as they occur.

The PSUs cliff vest on December 31, at the end of the third year from the date of grant. Share-based compensation expense is recognized on a straight-line basis over the service period of PSUs. The PSUs are subject to several service and market conditions, as defined by the PSU 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.

The Key Employee Awards cliff vest on December 31, 2023. Share-based compensation expense is recognized on a straight-line basis over the service period of the Key Employee Awards when it is probable that the performance conditions will be satisfied. The Key Employee Awards are subject to several service and performance conditions, as defined by the Key Employee Award agreement, which allows the holder to retain an amount of the awards as a result of certain termination conditions or change in common control. Forfeitures are accounted for as they occur.

14. 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 three months ended March 31, 2022 and 2021.

The Company matches 175% up to 6% of employee contributions of eligible compensation. Additionally, Plan participant forfeitures are used to reduce the cost of the Company contributions.

| | Three Months Ended | |
|--|---------------------------|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Contributions, net of forfeitures, made to the defined contribution plan | \$ 3,306 | \$ 2,280 |

Profit Sharing Bonus Plan

We maintain a discretionary profit sharing bonus plan under which approximately 10% of pre-tax profit from consolidated AAON Oklahoma and AAON Coil Products is paid to eligible employees on a quarterly basis in order to reward employee productivity. Eligible employees are regular full-time employees of AAON Oklahoma or AAON Coil Products 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 senior leadership team.

| | Three Months Ended | |
|-----------------------------------|---------------------------|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Profit sharing bonus plan expense | \$ 2,669 | \$ 2,132 |

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 | |
|-------------------------------------|---------------------------|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Medical claim payments | \$ 1,946 | \$ 1,813 |
| Health saving account contributions | 939 | 857 |

15. Earnings Per Share

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

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

| | Three Months Ended | |
|--|--|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands, except share and per share data)</i> | |
| Numerator: | | |
| Net income | \$ 18,059 | \$ 16,376 |
| Denominator: | | |
| Basic weighted average shares | 52,613,232 | 52,293,464 |
| Effect of dilutive shares related to stock based compensation ¹ | 927,137 | 1,521,180 |
| Effect of dilutive shares related to contingent consideration ² | 410,626 | — |
| Diluted weighted average shares | 53,950,995 | 53,814,644 |
| Earnings per share: | | |
| Basic | \$ 0.34 | \$ 0.31 |
| Dilutive | \$ 0.33 | \$ 0.30 |
| Anti-dilutive shares: | | |
| Shares | 437,636 | 100,625 |
| ¹ Dilutive shares related to stock options, restricted stock, PSUs and Key Employee Awards (Note 13) | | |
| ² Dilutive shares related to contingent shares issued to the former owners of BasX (Note 3 & Note 16) | | |

16. 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 in 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:

| Program | Three Months Ended | | | | | |
|-------------------------|--------------------|----------|--------------|----------------|----------|--------------|
| | March 31, 2022 | | | March 31, 2021 | | |
| | Shares | Total \$ | \$ per share | Shares | Total \$ | \$ per share |
| Open market | — | \$ — | \$ — | — | \$ — | \$ — |
| 401(k) | 54,305 | 3,278 | 60.36 | 70,350 | 5,185 | 73.70 |
| Directors and employees | 13,358 | 804 | 60.19 | 16,972 | 1,217 | 71.71 |
| Total | 67,663 | \$ 4,082 | \$ 60.33 | 87,322 | \$ 6,402 | \$ 73.31 |

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

| Program | Inception to March 31, 2022 | | |
|-------------------------|-----------------------------|------------|--------------|
| | Shares | Total \$ | \$ per share |
| Open market | 4,205,255 | \$ 74,793 | \$ 17.79 |
| 401(k) | 8,258,737 | 169,154 | 20.48 |
| Directors and employees | 2,041,085 | 23,145 | 11.34 |
| Total | 14,505,077 | \$ 267,092 | \$ 18.41 |

Subsequent to March 31, 2022 and through May 2, 2022, the Company repurchased a total of 16,692 shares for \$0.9 million from our 401(k) savings and investment plan and from our employees for payment of statutory tax withholdings on stock transactions.

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 17, 2021 | June 3, 2021 | July 1, 2021 | \$0.19 |
| November 9, 2021 | November 26, 2021 | December 17, 2021 | \$0.19 |

Contingent Shares Issued in BasX Acquisition

On December 10, 2021, we closed on the acquisition of BasX (Note 3). Under the MIPA Agreement, we committed to \$78.0 million in the aggregate of contingent consideration to the former owners of BasX, which is payable in approximately 1,037,000 shares of the Company's stock, par value \$0.004 per share. The shares do not accrue dividends.

Under the MIPA Agreement, the potential future issuance of the shares is contingent upon BasX meeting certain post-closing earn-out milestones during each of the years ended 2021, 2022, and 2023. Based on the final allocation of the consideration paid (Note 3), we estimated the fair value of contingent consideration related to these shares to be approximately \$60.0 million, which is included in additional paid-in capital on the consolidated balance sheets. As of March 31, 2022, 486,268 shares related to the year ended 2021 earn-out milestone had been issued to the former owners of BasX as part of a private placement exempt from registration with the SEC under Rule 506(b), which are included in common stock on the consolidated statements of stockholders' equity. No additional shares have been issued as of May 2, 2022.

17. 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 transactions in these VIEs outside of the financing transactions executed as part of the NMTC arrangement.

18. 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 March 31, 2022.

On April 27, 2022, the Company entered into a purchase sales agreement with a third party manufacturer to purchase the intellectual property rights to design and manufacture fan wheels for the purchase price of approximately \$6.5 million. The purchase price will be paid in three installments over the next 18 months. As of May 2, 2022 we have paid approximately \$1.0 million related to this agreement.

19. 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 for parts. 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. Through the acquisition of BasX (Note 3), at March 31, 2022, the Company leased an manufacturing and office facility in Redmond, Oregon from an entity in which certain members of management have an ownership interest.

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

| | Three Months Ended | |
|------------------------|-----------------------|----------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Sales to affiliates | \$ 752 | \$ 566 |
| Payments to affiliates | 364 | 73 |
| | March 31, 2022 | December 31, 2021 |
| | <i>(in thousands)</i> | |
| Due from affiliates | \$ 514 | \$ 547 |
| Due to affiliates | — | — |

20. Segments

The Company has determined that it has three reportable segments for financial reporting purposes. Management evaluates the performance of its business segments primarily on gross profit. The Company's chief decision maker ("CODM"), our CEO, allocates resources and assesses the performance of each operating segment using information about the operating segment's net sales and income from operations. The CODM does not evaluate operating segments using asset or liability information.

AAON Oklahoma: AAON Oklahoma designs, manufactures, sells and services standard, semi-custom and custom HVAC systems, designs and produces controls solutions for all of our HVAC units and sells retail parts to customers through our two retail part stores. Through the NAIC research and development laboratory facility, AAON Oklahoma is able test units under various environmental conditions. AAON Oklahoma includes the operations of both our Tulsa, Oklahoma and Parkville, Missouri facilities, our NAIC research and development laboratory facility and two retail parts locations.

AAON Coil Products: AAON Coil Products designs and manufactures a selection of our standard, semi-custom and custom HVAC systems. In addition, AAON Coil Products designs and manufactures various heating and cooling coils to be used in HVAC systems, mostly for the benefit of AAON Oklahoma and AAON Coil Products. AAON Coil Products consists of operations at our Longview, Texas facilities.

BasX: BasX provides product development design and manufacturing of custom engineered air handling systems including high efficiency data center cooling solutions, cleanroom solutions, HVAC systems and modular solutions. BasX consists of operations at our Redmond, Oregon facility.

The following table summarizes certain financial data related to our segments. Transactions between segments are recorded based on prices negotiated between the segments. The Gross Profit amounts shown below are presented after elimination entries.

| | Three Months Ended | |
|---------------------|---------------------------|-----------------------|
| | March 31, 2022 | March 31, 2021 |
| Net Sales | <i>(in thousands)</i> | |
| AAON Oklahoma | | |
| External sales | \$ 139,867 | \$ 99,976 |
| Inter-segment sales | 389 | 506 |
| AAON Coil Products | | |
| External sales | 21,935 | 15,812 |
| Inter-segment sales | 7,917 | 5,384 |
| BasX ¹ | 20,969 | — |
| Eliminations | (8,306) | (5,890) |
| Net sales | <u>\$ 182,771</u> | <u>\$ 115,788</u> |
| Gross Profit | | |
| AAON Oklahoma | \$ 33,836 | \$ 29,772 |
| AAON Coil Products | 7,306 | 3,385 |
| BasX ¹ | 4,922 | — |
| Gross profit | <u>\$ 46,064</u> | <u>\$ 33,157</u> |

¹ BasX was acquired on December 10, 2021.

| | March 31, 2022 | December 31, 2021 |
|---------------------------------------|-----------------------|--------------------------|
| Long-lived assets | <i>(in thousands)</i> | |
| AAON Oklahoma | \$ 190,621 | \$ 183,840 |
| AAON Coil Products | 63,957 | 62,534 |
| BasX | 28,654 | 28,662 |
| Total long-lived assets | <u>\$ 283,232</u> | <u>\$ 275,036</u> |
| Intangible assets and goodwill | | |
| AAON Oklahoma | \$ 3,229 | \$ 3,229 |
| AAON Coil Products | — | — |
| BasX | 145,973 | 152,619 |
| Total intangible assets and goodwill | <u>\$ 149,202</u> | <u>\$ 155,848</u> |

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, 2021.

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, 2021. 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, market, and sell premium air conditioning and heating equipment consisting of standard, semi-custom, and custom rooftop units, data center cooling solutions, cleanroom systems, chillers, packaged outdoor mechanical rooms, air handling units, makeup air units, energy recovery units, condensing units, geothermal/water-source heat pump, coils, and controls. These products are marketed and sold to retail, manufacturing, educational, lodging, supermarket, data centers, medical and pharmaceutical, and other commercial industries. We market our products to all 50 states in the United States and certain provinces in Canada. Foreign sales were approximately \$6.0 million of our total net sales for the three months ended March 31, 2022 and \$2.0 million of our sales during the same period of 2021.

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 in recent years. However, the recent rise in architectural billings and nonresidential building construction starts signal a 2022 recovery in nonresidential building construction after experiencing a downturn in 2021. Furthermore, general economic growth combined with pent-up demand from customers that delayed replacing old equipment is driving accelerated replacement demand. However, both the new construction and replacement markets are cyclical. If the domestic economy were to slow or enter a recession, this 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. Sales in the replacement markets are driven by various factors, including general economic growth, the Company's new product introductions, fluctuations in the average age of existing equipment in the market, government regulations and stimulus, changes in market demand between more customized higher performing HVAC equipment and lower priced standard equipment, as well as many other factors. When new construction is down, we emphasize the replacement market. 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.

We sell our products to property owners and contractors mainly through a network of independent manufacturers' representatives. This go-to-market strategy is unique compared to most of our larger competitors in that most control their sales channel. We value the independent sales channel as we think it is a more effective way of increasing market share. Although we concede full control of the sales process with this strategy, the entrepreneurial aspect of the independent sales channel attracts the most talent and provides greater financial incentives for its salespeople. Furthermore, the independent sales channel sells different types of equipment from various manufacturers, allowing it to operate with more of a solutions-based mindset, as opposed to an internal sales department of a manufacturing company that is incentivized to only sell its equipment regardless if it is the best solution for the end customer. We also have a small internal sales force that supports the relationships between the Company and our sales channel partners.

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.

The price levels of our raw materials fluctuate given that the market continues to be volatile and unpredictable as a result of the uncertainty related to the U.S. economy and global economy. At March 31, 2022, the price (twelve month trailing average) for copper, galvanized steel, stainless steel and aluminum increased 41.2%, 67.8%, 61.8%, and 1.6%, respectively, as compared to the price (twelve month trailing average) at March 31, 2021.

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.

We occasionally increase the price of our equipment to help offset any inflationary headwinds. In 2021, we implemented three price increases; and on January 1, 2022, we implemented a fourth price increase.

Recent Developments

On December 10, 2021, we closed on the acquisition of all of the issued and outstanding equity ownership of BasX, LLC, doing business as BasX Solutions ("BasX") (Note 3). We began including the results of BasX's operations in our consolidated financial statements beginning December 11, 2021.

On December 29, 2021, BasX, LLC converted to a C-Corporation, BasX, Inc., and is subject to income tax.

Backlog

The following table shows our historical backlog levels:

| <u>March 31, 2022</u> | <u>December 31, 2021</u> | <u>March 31, 2021</u> |
|---------------------------|------------------------------|---------------------------|
| <i>(in thousands)</i> | | |
| \$ 461,400 | \$ 260,164 | \$ 96,733 |

The Company has increased our backlog both through the acquisition of BasX and organic growth. Excluding BasX's backlog at March 31, 2022, organic backlog increased 305.0% compared to March 31, 2021, due in part to the completion of the Longview, Texas expansion in early 2021, price increases implemented throughout 2021 and our favorable lead times.

Results of Operations

| | Three months ended | |
|--|---------------------------|-----------------------|
| | <u>March 31, 2022</u> | <u>March 31, 2021</u> |
| | <i>(in thousands)</i> | |
| Net Sales | \$ 182,771 | \$ 115,788 |
| Cost of Sales | <u>136,707</u> | <u>82,631</u> |
| Gross Profit | 46,064 | 33,157 |
| Selling, general and administrative expenses | 23,056 | 14,696 |
| Gain on disposal of assets | (2) | — |
| Income from operations | <u>\$ 23,010</u> | <u>\$ 18,461</u> |

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 due primarily to strong end-market demand along with our ability to produce and meet customer lead times.

- Organic bookings increased 150% in the first quarter of 2022 compared to 2021 indicating a strong demand for our products.
- Sales in 2022 grew 57.8% to \$182.8 million due to organic volume growth of \$24.6 million, addition of BasX revenue of \$21.0 million, and price increases of \$16.5 million.
- Gross profit as a percentage of sales decreased in 2022 to 25.2% from 28.6% in 2021 due to the offset of increased sales by increased material costs and the adverse effect of supply chain issues on operations.
- Our warranty expense decreased 21.1% in the first quarter of 2022 compared to 2021 as a result of the quality control efforts the Company has put in place in the past few years.
- We continue to invest in the future growth of the Company evidenced by our \$14.0 million in capital expenditures.

We report our financial results based on three reportable segments: AAON Oklahoma, AAON Coil Products, and BasX, which are further described in "Segments" (Note 20) within our notes to the consolidated financial statements. The Company's chief decision maker ("CODM"), our CEO, allocates resources and assesses the performance of each operating segment using information about the operating segment's net sales and income from operations. The CODM does not evaluate operating segments using asset or liability information.

Segment Operating Results for Three Months Ended March 31, 2022 and Three Months Ended March 31, 2021

| | Three Months Ended | | | | \$ Change | % Change |
|----------------------------------|-----------------------|-------------------------------|----------------|-------------------------------|-----------|----------|
| | March 31, 2022 | Percent of Sales ² | March 31, 2021 | Percent of Sales ² | | |
| | <i>(in thousands)</i> | | | | | |
| Net Sales³ | | | | | | |
| AAON Oklahoma | \$ 139,867 | 76.5 % | \$ 99,976 | 86.3 % | \$ 39,891 | 39.9 % |
| AAON Coil Products | 21,935 | 12.0 % | 15,812 | 13.7 % | 6,123 | 38.7 % |
| BasX ¹ | 20,969 | 11.5 % | — | — | 20,969 | — |
| Net sales | \$ 182,771 | | \$ 115,788 | | \$ 66,983 | 57.8 % |
| Cost of Sales³ | | | | | | |
| AAON Oklahoma | \$ 106,031 | 75.8 % | 70,204 | 70.2 % | \$ 35,827 | 51.0 % |
| AAON Coil Products | 14,629 | 66.7 % | 12,427 | 78.6 % | 2,202 | 17.7 % |
| BasX ¹ | 16,047 | 76.5 % | — | — | 16,047 | — |
| Cost of sales | \$ 136,707 | 74.8 % | \$ 82,631 | 71.4 % | \$ 54,076 | 65.4 % |
| Gross Profit³ | | | | | | |
| AAON Oklahoma | \$ 33,836 | 24.2 % | \$ 29,772 | 29.8 % | \$ 4,064 | 13.7 % |
| AAON Coil Products | 7,306 | 33.3 % | 3,385 | 21.4 % | 3,921 | 115.8 % |
| BasX ¹ | 4,922 | 23.5 % | — | — | 4,922 | — |
| Gross profit | \$ 46,064 | 25.2 % | \$ 33,157 | 28.6 % | \$ 12,907 | 38.9 % |

¹ BasX was acquired on December 10, 2021. We have included the results of BasX's operations in our consolidated financial statements for the three months ended March 31, 2022.

² Cost of sales and gross profit for each segment are calculated as a percentage of the respective segment's net sales. Total cost of sales and total gross profit are calculated as a percentage of total net sales.

³ Presented after intercompany eliminations.

Total net sales increased \$67.0 million or 57.8%, due in part to increased organic volumes of \$24.6 million. The quarter also benefited from \$16.5 million of price increases put in place throughout 2021 that only now were realized. The acquisition of BasX in December 2021 added \$21.0 million to net sales for the three months ended March 31, 2021. AAON Coil Products saw a 40.0% increase in units sold, or approximately \$3.2 million, due to the increase in capacity with the completion of the new manufacturing building at our Longview, Texas facility in early 2021.

During the three months ended March 31, 2021, several production days were lost due to planned maintenance and due to impacts of bad weather at both AAON Oklahoma and AAON Coil Products, resulting in lower volumes. Additionally, the expansion at our Longview facility was completed and production began during the first quarter of 2021.

As shown in the table below, we've experienced increases in the cost of our raw materials. We implemented multiple price increases during 2021 and 2022 to counteract the increased cost of material. Additionally, in order to attract new employees, we increased starting wages for our production workforce by 7.0% in July 2021; and to retain our existing employees, we also put a cost of living increase of 3.5% in place in October 2021 for all employees below the Director level. In March 2022, we awarded annual merit raises for an overall 3.0% increase to wages. Additionally, during the first quarter of 2022, a review of the Company's useful lives for certain sheet metal manufacturing equipment at AAON Coil Products resulted in a change in estimate (Note 1) that increased the useful lives from between ten and twelve years to fifteen years. The change was made prospectively and resulted in a decrease to depreciation expense within cost of sales on our consolidated statements of income of \$1.8 million during the three months ended March 31, 2022.

Raw Material Costs

Twelve-month average raw material cost per pound as of March 31:

| | 2022 | | 2021 | | % Change |
|------------------|------|------|------|------|----------|
| Copper | \$ | 5.28 | \$ | 3.74 | 41.2 % |
| Galvanized steel | \$ | 0.99 | \$ | 0.59 | 67.8 % |
| Stainless steel | \$ | 2.33 | \$ | 1.44 | 61.8 % |
| Aluminum | \$ | 1.96 | \$ | 1.93 | 1.6 % |

Selling, General and Administrative Expenses

| | Three Months Ended | | Percent of Sales | | | |
|-----------------------------|-----------------------|-------------------|------------------|--------|--------|--------|
| | March 31, 2022 | March 31, 2021 | 2022 | 2021 | | |
| | <i>(in thousands)</i> | | | | | |
| Warranty | \$ | 1,157 | \$ | 1,467 | 0.6 % | 1.3 % |
| Profit sharing | | 2,669 | | 2,132 | 1.5 % | 1.8 % |
| Salaries & benefits | | 9,392 | | 5,034 | 5.1 % | 4.3 % |
| Stock compensation | | 1,669 | | 1,291 | 0.9 % | 1.1 % |
| Advertising | | 341 | | 206 | 0.2 % | 0.2 % |
| Depreciation & amortization | | 1,691 | | 699 | 0.9 % | 0.6 % |
| Insurance | | 709 | | 731 | 0.4 % | 0.6 % |
| Professional fees | | 1,482 | | 725 | 0.8 % | 0.6 % |
| Donations | | 189 | | (47) | 0.1 % | — % |
| Bad debt expense | | 288 | | (13) | 0.2 % | — % |
| Other | | 3,469 | | 2,471 | 1.9 % | 2.1 % |
| Total SG&A | \$ | 23,056 | \$ | 14,696 | 12.6 % | 12.7 % |

Excluding salaries and benefits at BasX of \$2.7 million, salaries and benefits increased \$1.6 million due to pay increases that went into effect during the second and third quarters of 2021. Additionally, profit sharing increased due to higher pre-tax income for the three months ended March 31, 2022. Depreciation and amortization expense at BasX was \$1.0 million, accounting for the majority of the change from period to period. Professional fees increased mostly due to continued transaction costs and audit fees.

Income Taxes

| | Three Months Ended | | Effective Tax Rate | |
|----------------------|-----------------------|-------------------|--------------------|--------|
| | March 31, 2022 | March 31, 2021 | 2022 | 2021 |
| | <i>(in thousands)</i> | | | |
| Income tax provision | \$ 4,782 | \$ 2,105 | 20.9 % | 11.4 % |

The Company's estimated annual 2022 effective tax rate, excluding discrete events, is expected to be approximately 25%. During the three months ended March 31, 2022, the Company recorded an excess tax benefit of \$0.5 million as compared to \$2.9 million during the same period in 2021, a decrease of 82.1%. 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.

Liquidity and Capital Resources

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

Working Capital - Our unrestricted cash increased \$2.8 million from December 31, 2021 to March 31, 2022 and totaled \$5.6 million at March 31, 2022.

Revolving Line of Credit - Our revolving credit facility ("Revolver"), as amended and restated, provides for maximum borrowings of \$100.0 million. As of March 31, 2022 and December 31, 2021, we had \$65.0 million and \$40.0 million, respectively, outstanding under the Revolver. We had one standby letter of credit totaling \$0.8 million as of March 31, 2022. At March 31, 2022, we have \$34.2 million of borrowings available under the Revolver. The Revolver expires November 24, 2026.

Any outstanding loans under the Revolver bear interest at the daily compounded secured overnight financing rate ("SOFR") plus the applicable margin. Applicable margin, ranging from 1.25% - 1.75%, is determined quarterly based on the Company's leverage ratio. The Company is also subject to letter of credit fees, ranging from 1.25% - 1.75%, and a commitment fee, ranging from 0.10% - 0.20%. The applicable fee percentage is determined quarterly based on the Company's leverage ratio. At March 31, 2022, the weighted average interest rate of the Revolver was 1.3%. Fees associated with the unused portion of the committed amount are included in interest expense on our consolidated statements of income and were not material for the three months ended March 31, 2022.

If SOFR cannot be determined pursuant to the definition, as defined by the Revolver agreement, any outstanding effected loans will be deemed to have been converted into alternative base rate ("ABR") loans. ABR loans would bear interest at a rate per annum equal to the highest of (a) the Prime Rate in effect on such day, (b) the Federal Funds Rate in effect on such day plus 0.50%, or (c) daily simple SOFR for a one-month tenor in effect on such day plus 1.00%.

At March 31, 2022, we were in compliance with our financial covenants, as defined by the Revolver. These covenants require that we meet certain parameters related to our leverage ratio. At March 31, 2022, our leverage ratio was 0.63 to 1.0, which meets the requirement of not being above 3 to 1.

As of May 5, 2022, we had \$75.0 million of outstanding borrowings under our Revolver.

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 in 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:

| Program | Three Months Ended | | | | | |
|--|--------------------|----------|--------------|----------------|----------|--------------|
| | March 31, 2022 | | | March 31, 2021 | | |
| | Shares | Total \$ | \$ per share | Shares | Total \$ | \$ per share |
| <i>(in thousands, except share and per share data)</i> | | | | | | |
| Open market | — | \$ — | \$ — | — | \$ — | \$ — |
| 401(k) | 54,305 | 3,278 | 60.36 | 70,350 | 5,185 | 73.70 |
| Directors and employees | 13,358 | 804 | 60.19 | 16,972 | 1,217 | 71.71 |
| Total | 67,663 | \$ 4,082 | \$ 60.33 | 87,322 | \$ 6,402 | \$ 73.31 |

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

| Program | Inception to March 31, 2022 | | |
|--|-----------------------------|------------|--------------|
| | Shares | Total \$ | \$ per share |
| <i>(in thousands, except share and per share data)</i> | | | |
| Open market | 4,205,255 | \$ 74,793 | \$ 17.79 |
| 401(k) | 8,258,737 | 169,154 | 20.48 |
| Directors and employees | 2,041,085 | 23,145 | 11.34 |
| Total | 14,505,077 | \$ 267,092 | \$ 18.41 |

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 17, 2021 | June 3, 2021 | July 1, 2021 | \$0.19 |
| November 9, 2021 | November 26, 2021 | December 17, 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 2022 and the foreseeable future.

Statement of Cash Flows

The following table reflects the major categories of cash flows for the three months ended March 31, 2022 and 2021. For additional details, see the consolidated financial statements.

| | Three Months Ended | |
|---|---------------------------|---------------------------|
| | March 31, 2022 | March 31, 2021 |
| | <i>(in thousands)</i> | |
| Operating Activities | | |
| Net Income | \$ 18,059 | \$ 16,376 |
| Income statement adjustments, net | 11,730 | 14,606 |
| Changes in assets and liabilities: | | |
| Accounts receivable | (43,244) | (5,179) |
| Income taxes | 3,631 | (2,766) |
| Inventories | (16,041) | (1,627) |
| Contract assets | (4,252) | — |
| Prepaid expenses and other | (3,588) | 108 |
| Accounts payable | 6,325 | 4,904 |
| Contract liabilities | 17,998 | — |
| Deferred revenue | 68 | 2,358 |
| Accrued liabilities & donations | 2,511 | 58 |
| Net cash (used in) provided by operating activities | <u>(6,803)</u> | <u>28,838</u> |
| Investing Activities | | |
| Capital expenditures | (14,031) | (16,404) |
| Cash paid in business combination, net of cash acquired | (249) | — |
| Other | 16 | 14 |
| Net cash used in investing activities | <u>(14,264)</u> | <u>(16,390)</u> |
| Financing Activities | | |
| Borrowings under revolving credit facility. | 25,000 | — |
| Stock options exercised | 2,890 | 9,438 |
| Repurchase of stock | (3,278) | (5,185) |
| Employee taxes paid by withholding shares | (804) | (1,217) |
| Net cash provided by financing activities | <u>\$ 23,808</u> | <u>\$ 3,036</u> |

Cash Flows Provided by Operating Activities

The Company currently manages cash needs through working capital as well as 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 decrease in cash flows from receivables was a result of increased sales, both as a result of 2021 price increases realized during the period and volumes, in the three months ended March 31, 2022 that have not been collected. The Company has also increased the purchase of inventory to take advantage of favorable pricing opportunities and also to mitigate the impact of future supply chain disruptions on our operations.

Cash Flows Used in Investing Activities

The capital expenditures for the three months ended March 31, 2022 relate to our continued investment in our production capabilities. The capital expenditures for the three months ended March 31, 2021 related to the completion of the expansion at our Longview, Texas facility, which became operational during early 2021. The capital expenditure program for 2022 is estimated to be approximately \$100.4 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

Cash flows from financing activities is historically affected by the timing of stock options exercised by our employees and repurchases of the Company's stock. However, the increase in cash from financing activities is primarily related to borrowings under our revolving credit facility to manage our working capital needs, especially strategic purchases of inventory to avoid future supply chain delays, after our available cash on hand was used to fund the BasX acquisition. Stock options exercised decreased due to the decrease in the number of employee options exercised and decrease in our average stock price during the three months ended March 31, 2022 compared to the three months ended March 31, 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 March 31, 2022.

Critical Accounting Policies

There have been no material changes in the Company's critical accounting policies during the three months ended March 31, 2022.

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, 2021. 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 2021 Annual Report.

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. From inception through March 31, 2022, 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 March 31, 2022, we repurchased approximately 8.3 million shares (at current market prices) for an aggregate price of \$169.2 million, or an average price of \$20.48 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 March 31, 2022, we repurchased approximately 2.0 million shares (at current market prices) for an aggregate price of \$23.1 million, or an average price of \$11.34 per share.

Repurchases during the first quarter of 2022 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 |
|---------------|--|---|---|---|
| January 2022 | 22,159 | \$ 68.36 | 22,159 | — |
| February 2022 | 18,315 | 59.34 | 18,315 | — |
| March 2022 | 27,189 | 54.40 | 27,189 | — |
| Total | 67,663 | \$ 60.33 | 67,663 | — |

Under the membership interest purchase agreement ("MIPA Agreement") entered into for the acquisition of BasX, LLC ("BasX," Note 3), we committed to \$78.0 million in the aggregate of contingent consideration to the former owners of BasX, which is payable in approximately 1,037,000 shares of the Company's stock, par value \$0.004 per share. Under the MIPA Agreement, the potential future issuance of the shares is contingent upon BasX meeting certain post-closing earn-out milestones during each of the years ended 2021, 2022, and 2023. As of March 31, 2022, 486,268 shares related to the year ended 2021 earn-out milestone had been issued to the former owners of BasX as part of a private placement exempt from registration with the SEC under Rule 506(b). No additional shares have been issued as of May 2, 2022.

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.

| <u>Exhibit #</u> | <u>Description</u> |
|-----------------------------|--|
| <u>31.1</u> | 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. |
| <u>31.2</u> | 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. |
| <u>32.1</u> | 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. |
| <u>32.2</u> | 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 March 31, 2022 and December 31, 2021; (ii) our Consolidated Statements of Income for the three and three months ended March 31, 2022 and 2021; (iii) our Consolidated Statements of Stockholders' Equity for the three and three months ended March 31, 2022 and 2021; (iv) our Consolidated Statements of Cash Flows for the three months ended March 31, 2022 and 2021; 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: May 05, 2022

By: _____
/s/ Gary D. Fields
Gary D. Fields
Chief Executive Officer

Dated: May 05, 2022

By: _____
/s/ Rebecca A. Thompson
Rebecca A. Thompson
Chief Financial Officer

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: May 05, 2022

/s/ Gary D. Fields

Gary D. Fields
Chief Executive Officer

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: May 05, 2022

/s/ Rebecca A. Thompson

Rebecca A. Thompson
Chief Financial Officer

**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 March 31, 2022, 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: May 05, 2022

/s/ Gary D. Fields

Gary D. Fields
Chief Executive Officer

**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 March 31, 2022, 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: May 05, 2022

/s/ Rebecca A. Thompson

Rebecca A. Thompson
Chief Financial Officer