

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

FORM 10QSB

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

For the quarterly period ended September 30th 2004

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

FLEXIBLE SOLUTIONS INTERNATIONAL INC.

(Exact name of small business issuer as specified in its charter)

NEVADA

(State or other jurisdiction of incorporation or organization)

91-1922863

(IRS Employer Identification No.)

615 Discovery Street, Victoria BC V8T 5G4

(Address of principal executive offices)

( 250 ) 477 - 9969

(Issuer's telephone number)

(Former name, former address and former fiscal year if changed since last report)

**APPLICABLE ONLY TO ISSUERS INVOLVED IN BANKRUPTCY  
PROCEEDINGS DURING THE PRECEDING FIVE YEARS**

Check whether the registrant filed all documents and reports required to be filed by Section 12,13 or 15(d) of the Exchange Act after the distribution of securities under a plan confirmed by a court. Yes [ ] No [ ]

**APPLICABLE ONLY TO CORPORATE ISSUERS**

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: Common stock \$.001 par value 11,831,916 shares as of Oct 29<sup>th</sup> 2004.

Transitional Small Business Disclosure Format (Check one): Yes [ ] No [X]

## PART I - FINANCIAL INFORMATION

### Item 1. FINANCIAL STATEMENTS.

Attached hereto and incorporated herein by reference.

### Item 2. MANAGER'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following information contains certain forward-looking statements that anticipate future trends or events. These statements are based on certain assumptions that may prove to be erroneous and are subject to certain risks including but not limited to the risks of increased competition in the Company's industry and other risks detailed in the Company's Securities and Exchange Commission filings. Accordingly, actual results may differ, possibly materially, from the predictions contained herein.

#### RESULTS OF OPERATIONS

The following analysis and discussion pertains to the Company's results of operations for the three month and nine month periods ended Sept. 30<sup>th</sup> 2004, compared to the results of operations for the three month and nine month periods ended Sept. 30<sup>th</sup> 2003, and to changes in the Company's financial condition from December 31<sup>st</sup> 2003 to Sept. 30<sup>th</sup> 2004.

#### THREE MONTHS ENDED September 30<sup>th</sup> 2004 and 2003

For the three months ended Sept. 30<sup>th</sup> 2004, the Company experienced a loss of \$154,090 as compared to a loss of \$290,254 for the three months ended Sept. 30<sup>th</sup> 2003. Although swimming pool product sales were negatively impacted by the end of the northeastern season and the transition from outside to inside distribution, increases in pool product sales outside of North America and a full quarter of operations from the NanoChem division resulted in revenue of \$1,376,054 compared to \$40,009 in the year earlier quarter. Management is extremely satisfied with the effect of the acquisition. The NanoChem division contributed greatly to sales and cash flow only 110 days after the close and is starting to replace the capital expended for it. As well, opportunities to synergistically cross sell the products of all divisions have already generated leads to new business and the swimming pool division has discovered ways to help NanoChem increase utilization of the Peru, IL factory while decreasing costs for the Company as a whole. The Company maintained expenditures in the areas of WaterSavr sales and marketing and production equipment development. The major changes that resulted in the large revenue increase were greater sales from our swimming pool division into new overseas markets and the first complete quarter of sales from the recently acquired NanoChem division. NanoChem sales are much less seasonal than those of our WaterSavr and Flexible Solutions Ltd divisions which should lead to less volatile sales figures in future. Management will attempt to reduce seasonality even further over time.

Operating expenses were \$1,114,831 for the third quarter, up from \$372,725 for the third quarter of 2003. Flexible Solutions continued expanding its sales and marketing efforts for WaterSavr with the objective of closing the first major sales as soon as possible and with development of advanced production machinery for swimming pool products. The largest real increases were in the areas of wages (\$349,226 versus \$74,786), rent, (\$62,495 versus \$11,601), office (\$62,099 from \$24,559), and consulting, (105,293 versus 39,572). These increases are wholly accounted for by the operating costs of the new division and represent a permanent increase in operating costs related to the new level of sales. The decreases in travel, (\$30,317 versus \$41,611) and advertising (\$16,466 down from \$31,757) are the result of better-cost control in these areas instituted by management over the past year. Professional fees increased to \$104,432 from \$45,270 in the quarter. This was largely the result of the one-time costs of transferring patent assets of the acquisition. In addition, a substantial amount of the increase in consulting fees, from \$39,572 to \$105,293, is the result of expensing of consultant options. Note should be made that depreciation increased to \$173,989 from \$8,841 as a result of the depreciable NanoChem assets acquired in June 2004.

The loss for the quarter was \$154,090, a decrease from third quarter last year when the loss was \$290,254. The decreased loss was realized through increased sales in swimming pool products compared to the year earlier quarter augmented by positive operating cash from the NanoChem division.

The loss per share was \$0.01 for the three months ended September 30<sup>th</sup> 2004 compared to a loss of \$0.02 for the three months ended September 30<sup>th</sup> 2003.

### **NINE MONTHS ENDED September 30<sup>th</sup> 2004 and 2003**

Sales in the nine months ended September 30<sup>th</sup> 2004 were \$2,411,925 compared to \$1,982,571 for the nine months ended September 30<sup>th</sup> 2003. The swimming pool division experienced temporarily reduced sales as a result of taking over distribution from an outside group. The product pipeline was filled prior to the distribution change and the focus of our sales team was directed toward ensuring sales for the 2005 season and expanding sales overseas. However, 20 days of revenue in second quarter and the full third quarter from the NanoChem division combined with reasonable sales in the swimming pool products line resulted in nine month sales of \$2,411,925, an increase of 22%.

Operating expenses for the Company were \$2,348,314 for the nine months ended September 30<sup>th</sup> 2004 up from \$1,346,863 for the nine months ended Sept. 30<sup>th</sup> 2003. The increase in operating expenses was a result of the increase in total sales. The loss for the nine months ended September 30<sup>th</sup> 2004 was \$732,239 compared to a loss of \$339,026 for the nine months ended September 30<sup>th</sup> 2003. Of the increased loss, \$329,007 was from depreciation on the assets of the acquisition and \$206,957 was from expensing of consultant options.

The loss per share was \$0.06 for the nine-month period ended September 30<sup>th</sup> 2004 compared to a loss of \$0.03 for the nine-month period ended September 30<sup>th</sup> 2003.

### **LIQUIDITY AND CAPITAL RESOURCES**

The Company has cash on hand of \$774,324 as of the end of Sept 2004 compared to \$141,435 on Sept 30<sup>th</sup> 2003.

As of September 30<sup>th</sup> 2004 the Company had working capital of \$241,553 as compared to working capital of \$5,857,728 on December 31<sup>st</sup> 2003. The decrease was a result of the cash used to purchase the assets that have become the NanoChem division and the costs associated with that acquisition combined with the continuing costs of market development for the WaterSavr division.

The Company has no external sources of liquidity in the form of credit lines from banks.

Management believes that its available cash will be sufficient to fund the Company's working capital requirements through December 31<sup>st</sup> 2004. Management further believes that available cash will be sufficient to implement the Company's expansion plans. No investment banking agreements are in place and there is no guarantee that the Company will be able to raise capital in the future should that become necessary.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS:**

The Company does not have any derivative financial instruments as of September 30<sup>th</sup> 2004. However, the Company is exposed to interest rate risk.

The Company's interest income and expense are most sensitive to changes in the general level of U.S. and Canadian interest rates. In this regard, changes in U.S. and Canadian interest rates affect the interest paid on the Company's cash equivalents as well as the interest paid on debt.

### **FOREIGN CURRENCY RISK**

The Company operates extensively in both Canada and the USA. Therefore, the Company's business and financial condition is sensitive to currency exchange rates or any other restriction imposed on its currency.

## Part II - OTHER INFORMATION

- Item 1. Legal proceedings – The Company is plaintiff in a lawsuit demanding the return of the share certificate of 100,000 shares of stock originally given as payment in advance for services, \$10,000 and undetermined damages resulting from a breach of contract. The suit has been filed in Circuit Court of Cook County, IL against Tatko Biotech Inc. of Peoria, IL. The services for which the advance was given were never performed or given to the company, and the company therefore received no consideration or value for such advance.
- Item 2. Changes in Securities  
None
- Item 3. Default upon Senior Securities - None
- Item 4. Submission of Matters to a Vote of Securities Holders - None
- Item 5. Other Information - None
- Item 6.(b) Reports on Form 8-K  
October 6<sup>th</sup>, 2004 – Financial results  
August 23, 2004 – Legal proceedings  
July 26, 2004 -- Appointed Officer

### Item 14. Controls and procedures

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure based closely on the definition of "disclosure controls and procedures" in Rule 13a-14(c). In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Within 90 days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on the foregoing, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

There have been no significant changes in the Company's internal controls or in other factors that could significantly affect the internal controls subsequent to the date the Company completed its evaluation.

## 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.

FLEXIBLE SOLUTIONS INTERNATIONAL INC.  
(Registrant)

Dated: November 12<sup>th</sup> 2004

/s/ Dan O'Brien, President and Director

EXHIBIT 31.1

1. I have reviewed this quarterly report on Form 10-QSB of Flexible Solutions International Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) Designed such disclosure controls and procedures 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 quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, 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 in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 12<sup>th</sup> 2004

/s/Dan O'Brien  
Dan O'Brien  
CEO

EXHIBIT 31.2

I, Fred Kupel, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Flexible Solutions International Inc.;
2. Based on my knowledge, this quarterly 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 quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) Designed such disclosure controls and procedures 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 quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, 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 in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 12<sup>th</sup> 2004

/s/Fred Kupel  
Fred Kupel  
CFO

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

In connection with the quarterly report of Flexible Solutions International Inc. on form 10-Q for the period ended September 30<sup>th</sup> 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Dan O'Brien, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. 1350, as adopted pursuant to section 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 results of operations of the Company.

/s/ Dan O'Brien  
Dan O'Brien  
CEO, Nov 12<sup>th</sup> 2004

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

In connection with the quarterly report of Flexible Solutions International Inc. (the Company) on form 10-Q for the period ended September 30<sup>th</sup> 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Dan O'Brien, Chief Financial Officer of the Company, certify pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of Section 13(a) or 15(b) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly represents, in all material respects, the financial condition and results of operations of the Company.

/s/ Fred Kupel  
Fred Kupel  
CFO, November 12<sup>th</sup> 2004

**FLEXIBLE SOLUTIONS INTERNATIONAL INC.****Consolidated Balance Sheets****September 30, 2004****(Unaudited - U.S. Dollars)**

	<b>September 30 2004</b>	<b>December 31 2003</b>
<b>Assets</b>		
<b>Current</b>		
Cash and cash equivalents	\$ 774,324	\$ 237,080
Short term investments	938,360	5,033,837
Accounts receivable	591,524	294,238
Income tax receivable	85,123	86,243
Loan receivable	17,849	17,585
Inventory	1,009,891	212,938
Prepaid expenses	134,279	36,101
	3,551,350	5,918,022
<b>Property and equipment</b>	<b>5,207,929</b>	<b>167,589</b>
<b>Investment</b>	<b>303,500</b>	<b>303,500</b>
	<b>\$ 9,062,779</b>	<b>\$ 6,389,111</b>
<b>Liabilities</b>		
<b>Current</b>		
Due to shareholders	-	7,700
Short term loan	3,150,000	-
Accounts payable and accrued liabilities	159,817	\$ 157,643
	3,309,817	165,343
<b>Stockholders' Equity</b>		
<b>Capital stock</b>		
Authorized		
50,000,000 Common shares with a par value of \$0.001 each		
1,000,000 Preferred shares with a par value of \$0.01 each		
Issued and Outstanding		
11,831,916 (2003: 11,794,916) common shares	11,832	11,794
<b>Capital in excess of par Value</b>	<b>7,571,032</b>	<b>7,306,613</b>
<b>Other comprehensive income (loss)</b>	<b>-</b>	<b>3,023</b>
<b>Deficit</b>	<b>(1,829,903)</b>	<b>(1,097,662)</b>
<b>Total Stockholder's Equity</b>	<b>5,752,961</b>	<b>6,223,768</b>
<b>Total Liabilities and Stockholder's Equity</b>	<b>\$ 9,062,778</b>	<b>\$ 6,389,111</b>

**FLEXIBLE SOLUTIONS INTERNATIONAL INC.****Consolidated Statements of Operations****Nine Months Ended September 30, 2004 and 2003****(Unaudited - U.S. Dollars)**

	<b>Nine Months Ended September 30</b>	
	<b>2004</b>	<b>2003</b>
<b>Sales</b>	\$ 2,411,925	\$ 1,982,571
<b>Cost of sales</b>	829,314	1,130,293
<b>Gross profit</b>	1,582,611	852,278
<b>Operating Expenses</b>		
Wages	606,942	408,658
Administrative salaries and benefits	94,973	60,258
Advertising and promotion	73,258	60,915
Investor relations and transfer agent fee	173,164	120,273
Office and miscellaneous	154,053	59,334
Insurance	33,475	-
Interest expense	29,364	-
Rent	114,711	49,153
Consulting	294,109	122,223
Professional fees	212,146	173,143
Travel	79,831	120,030
Telecommunications	28,464	36,576
Shipping	21,950	14,687
Research	21,000	61,298
Bad debt expense (recovery)	(797)	822
Currency exchange	5,666	20,787
Utilities	46,469	13,938
Depreciation	359,536	24,768
	2,348,314	1,346,863
<b>Income (loss) before interest income and income tax</b>	(765,704)	(494,585)
<b>Interest income</b>	33,464	155,196
<b>Income (loss) before income tax</b>	(732,239)	(339,389)
<b>Income tax (recovery)</b>		(363)
<b>Net income (loss)</b>	(732,239)	\$ (339,026)
<b>Deficit, beginning</b>	(1,097,662)	(3,100,974)
<b>Deficit, ending</b>	(1,829,901)	(3,440,000)
<b>Net income (loss) per share</b>	(0.06)	(0.03)
<b>Weighted average number of shares</b>	11,826,345	11,715,619

**FLEXIBLE SOLUTIONS INTERNATIONAL INC.**  
**Consolidated Statements of Operations**  
**Three Months Ended September 30, 2004 and 2003**  
**(Unaudited - U.S. Dollars)**

	<b>Three Months Ended September 30</b>	
	<b>2004</b>	<b>2003</b>
<b>Sales</b>	\$ 1,376,054	\$ 40,009
<b>Cost of sales</b>	418,307	34,944
<b>Gross profit</b>	957,747	5,065
<b>Operating Expenses</b>		
Wages	349,226	74,786
Administrative salaries and benefits	37,429	20,783
Advertising and promotion	16,466	31,757
Investor relations and transfer agent fee	50,539	51,606
Office and miscellaneous	62,099	24,559
Insurance	28,507	-
Interest expense	29,364	-
Rent	62,495	11,601
Consulting	105,293	39,572
Professional fees	104,432	45,270
Travel	30,317	41,611
Telecommunications	13,750	11,976
Shipping	11,153	6,409
Research	5,158	41,594
Bad debt expense (recovery)	-	822
Currency exchange	2,343	(42,172)
Utilities	32,271	3,711
Depreciation	173,989	8,841
	1,114,831	372,726
<b>Income (loss) before interest income and income tax</b>	(157,084)	(367,661)
<b>Interest income</b>	2,994	50,950
<b>Income (loss) before income tax</b>	(154,090)	(316,711)
<b>Income tax (recovery)</b>		(26,457)
<b>Net income (loss)</b>	(154,090)	\$ (290,254)
<b>Deficit, beginning</b>	(1,675,812)	\$ (3,149,746)
<b>Deficit, ending</b>	(1,829,902)	\$ (3,440,000)
<b>Net income (loss) per share</b>	(0.01)	(0.02)
<b>Weighted average number of shares</b>	11,831,916	11,791,612

**FLEXIBLE SOLUTIONS INTERNATIONAL INC.**  
**Consolidated Statements of Cash Flows**  
**For The Nine Months Ended September 30, 2004 and 2003**  
**(Unaudited - U.S. Dollars)**

	<b>Nine Months Ended September 30</b>	
	<b>2004</b>	<b>2003</b>
<b>Operating activities</b>		
Net income (loss)	\$ (732,241)	\$ (339,026)
Stock compensation expense	206,957	68,998
Depreciation	359,536	24,768
Changes in non-cash working capital items:		
Accounts receivable	(297,286)	(170,996)
Inventory	(796,953)	(23,462)
Prepaid expenses	(98,177)	34,685
Accounts payable	2,174	12,796
Income tax receivable	1,120	60,014
Decrease in due to shareholders	(7,700)	-
Unrealized foreign exchange gain/loss	-	-
<b>Cash provided by (used in) operating activities</b>	<b>(1,362,571)</b>	<b>(332,223)</b>
<b>Investing activities</b>		
Acquisition of property and equipment	(5,399,876)	(49,477)
Short-term investments	4,095,477	(143,683)
Loan receivable	(264)	(277,625)
Acquisition of investments	-	(1,827)
<b>Cash used in investing activities</b>	<b>(1,304,663)</b>	<b>(472,612)</b>
<b>Financing activity</b>		
Subscriptions received	-	3,000
Short term loan	3,150,000	
Proceeds from issuance of common stock	57,500	401,058
<b>Cash provided by financing activities</b>	<b>3,207,500</b>	<b>404,058</b>
Effect of exchange rate changes on cash	(3,022)	(14,576)
<b>Inflow (outflow) of cash</b>	<b>537,244</b>	<b>(415,353)</b>
Cash and cash equivalents, beginning of period	237,080	556,789
<b>Cash and cash equivalents, end of period</b>	<b>\$ 774,324</b>	<b>\$ 141,436</b>
<b>Supplemental disclosure of cash flow information:</b>		
Income taxes paid	\$ -	\$ 58,000
Interest received	33,464	155,196

# **FLEXIBLE SOLUTIONS INTERNATIONAL INC.**

## **Notes to Consolidated Financial Statements**

**Periods Ended September 30**

**(U.S. Dollars)**

**(Unaudited)**

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### **1. BASIS OF PRESENTATION**

These unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States for interim financial information. These financial statements are condensed and do not include all disclosures required for annual financial statements. The organization and business of the Company, accounting policies followed by the Company and other information are contained in the notes to the Company's audited consolidated financial statements filed as part of the Company's December 31, 2003 Annual Report on Form 10-KSB. This quarterly report should be read in conjunction with such annual report.

In the opinion of the Company's management, these consolidated financial statements reflect all adjustments necessary to present fairly the Company's consolidated financial position at September 30, 2004 and the consolidated results of operations and the consolidated statements of cash flows for the nine months ended September 30, 2004 and 2003. The results of operations for the three months ended September 30, 2004 are not necessarily indicative of the results to be expected for the entire fiscal year.

### **2. SIGNIFIGANT ACCOUNTING POLICIES**

These consolidated financial statements have been prepared in accordance with generally accepted accounting principles accepted in the United States of America applicable to a going concern and reflect the policies outlined below.

#### **a) Cash and Cash Equivalents -**

The company considers all highly liquid investments purchased with an original or remaining maturity of less than three months at the date of purchase to be cash equivalents. Cash and cash equivalents are maintained with several financial institutions.

#### **b) Inventory -**

Inventory is valued at the lower of cost and net realizable value. Cost is determined on a first-in, first-out basis.

#### **c) Property, Equipment and Leaseholds -**

The following assets are recorded at cost and depreciated using the following methods using the following annual rates:

Computer hardware	30% Declining balance
Furniture and fixtures	20% Declining balance
Manufacturing equipment	20% Declining balance
Office equipment	20% Declining balance
Trailer	30% Declining balance
Building	10% Declining balance
Leasehold improvements	Straight-line over lease term

Property and equipment are written down to net realizable value when management determines there has been a change in circumstances, which indicates its carrying amount, may not be recoverable. No write-downs have been necessary to date.

## **FLEXIBLE SOLUTIONS INTERNATIONAL INC.**

### **Notes to Consolidated Financial Statements**

**Periods Ended September 30**

**(U.S. Dollars)**

**(Unaudited)**

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d) Foreign Currency -

The functional currency of the company is the Canadian dollar. The translation of the Canadian dollar to the reporting currency of the U.S. dollar is performed for assets and liabilities using exchange rates in effect at the balance sheet date. Revenue and expense transactions are translated using average exchange rates prevailing during the year. Translation adjustments arising on conversion of the financial statements from the company's functional currency, Canadian dollars, into the reporting currency, U.S. dollars, are excluded from the determination of income and disclosed as other comprehensive income (loss) in stockholders' equity.

Foreign exchange gains and losses relating to transactions not denominated in the applicable local currency are included in income if realized during the year and in comprehensive income if they remain unrealized at the end of the year.

e) Revenue Recognition -

Revenue from product sales is recognized at the time the product is shipped since title and risk of losses is transferred to purchaser upon delivery to the carrier. Shipments are made F.O.B. shipping point. Provisions are made at the time the related revenue is recognized for estimated product returns. Since the company's inception, product returns have been insignificant, therefore no provision has been established for estimated product returns.

f) Stock Issued in Exchange for Services -

The valuation of the common stock issued in exchange for services is valued at an estimated fair market value as determined by officers and directors of the company based upon trading prices of the company's common stock on the dates of the stock transactions.

g) Stock Based Compensation -

The company applies APB Opinion No. 25 and related interpretations in accounting for its employee stock option plans. Compensation expense is recorded when options are granted to management at discounts to market.

h) Comprehensive Income -

Other comprehensive income refers to revenues, expenses, gains and losses that under generally accepted accounting principles are included in comprehensive income but are excluded from net income as these amounts are recorded directly as an adjustment to stockholders' equity. The company's other comprehensive income is primarily comprised of unrealized foreign exchange gains and losses.

i) Income (Loss) Per Share -

Income (loss) per share is calculated by dividing net income (loss) by the weighted average number of shares outstanding.

## **FLEXIBLE SOLUTIONS INTERNATIONAL INC.**

### **Notes to Consolidated Financial Statements**

**Periods Ended September 30**

**(U.S. Dollars)**

**(Unaudited)**

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j) Use of Estimates -

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates and would impact the results of operations and cash flows.

k) Financial Instruments -

The fair market value of the company's financial instruments comprising cash, short-term investment, accounts receivable, income tax recoverable, loan receivable, accounts payable and accrued liabilities and amounts due to shareholders were estimated to approximate their carrying values due to immediate or short-term maturity of these financial instruments.

The company is exposed to foreign exchange and interest rate risk to the extent that market value rate fluctuations materially differ from financial assets and liabilities subject to fixed long-term rates.

l) Recent Accounting Pronouncements -

i) In June 2001, the Financial Accounting Standards Board (FASB) issued FAS 142, Goodwill and Other Intangible Assets. Under FAS 142, goodwill and intangible assets with indefinite lives are no longer amortized but are reviewed at least annually for impairment. The amortization provisions of FAS 142 apply to goodwill and intangible assets acquired after June 30, 2001. With respect to goodwill and intangible assets acquired prior to July 1, 2001, the company adopted FAS 142 effective January 1, 2002. Application of the non-amortization provisions of FAS 142 for goodwill did not have any impact on its financial reporting

ii) In October 2001, the FASB issued Statement of Financial Accounting Standards for FAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." FAS 144 addresses significant issues relating to the implementation of FAS 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of," and develops a single accounting model, based on the framework established in FAS 121 for long-lived assets to be disposed of by sale, whether such assets are or are not deemed to be a business. FAS 144 also modifies the accounting and disclosure rules for discontinued operations. The standard was adopted on January 1, 2002 and did not have any impact on the financial statements.

In November 2001, the FASB issued EITF Issue No. 01-14, "Income Statement Characterization of Reimbursements Received for "Out of Pocket" Expenses Incurred." This guidance requires companies to recognize the recovery of reimbursable expenses such as travel costs on service contracts as revenue. These costs are not to be netted as a reduction of cost. This guidance was implemented January 1, 2002. The company does not expect this guidance to have a material impact on the financial statements

## FLEXIBLE SOLUTIONS INTERNATIONAL INC.

Notes to Consolidated Financial Statements

Periods Ended September 30

(U.S. Dollars)

(Unaudited)

### 3. PROPERTY, EQUIPMENT AND LEASEHOLDS:

	Cost	Accumulated Amortization	September 2004 Net	December 2003 Net
Computer hardware	\$ 36,371	\$ 11,692	\$ 24,680	\$ 9,267
Furniture and equipment	14,278	3,197	11,080	3,293
Office equipment	27,339	9,231	18,108	15,195
Manufacturing equipment	2,037,063	291,093	1,745,970	133,283
Trailer	1,763	577	1,186	1,518
Building	3,144,259	153,754	2,990,507	-
Leasehold improvements	23,610	9,227	14,382	5,033
Trade show display	4,140	310	3,830	-
Land	398,186	-	398,186	-
	<u>\$ 5,687,009</u>	<u>\$ 479,081</u>	<u>\$ 5,207,929</u>	<u>\$ 167,589</u>

### 4. STOCKHOLDERS' EQUITY

- (a) During the prior periods, the Company granted stock options to consultants and have recognized consulting expense applying SFAS 123 using the Black-Scholes option-pricing model, which resulted in expense of \$71,727 for the three months, ended September 30, 2004.
- (b) The following table summarizes the Company's stock option activity for the period:

	2004		
	Number of Shares	Exercise Price Per Share	Weighted Average Exercise Price
Balance, June 30, 2004	1,758,740	\$ 1.00 to \$ 4.55	\$ 2.79
Granted During the Period	5,000	\$3.60	3.60
Exercised	0	0	0
Cancelled	500,000	\$2.50 to \$3.50	\$3.10
Balance, September 30, 2004	1,263,740	\$ 1.00 to \$ 4.25	\$ 2.67

## **FLEXIBLE SOLUTIONS INTERNATIONAL INC.**

**Notes to Consolidated Financial Statements**

**Periods Ended September 30**

**(U.S. Dollars)**

**(Unaudited)**

### **5. ACQUISITION OF ASSETS OF DONLAR CORPORATION**

Pursuant to a purchase agreement dated May 26, 2004, the company acquired the assets of Donlar Corporation on June 9, 2004.

The purchase price of the transaction was \$6,150,000 with consideration being a combination of cash and debt. Under the purchase agreement and as part of the consideration, the company issued a promissory note bearing interest at the prime rate to the vendor to satisfy \$3,150,000 of the purchase price.

The following table summarizes the estimated fair value of the assets acquired at the date of acquisition:

As at June 9, 2004:

Current assets	\$ 1,126,805
Property and equipment	5,023,195
	<u>\$ 6,150,000</u>
Acquisitions costs assigned to property and equipment	254,874
Total assets acquired	<u><u>\$ 6,404,874</u></u>

### **6. CONTINGENCIES**

- a) The Company has been named as a defendant in a lawsuit filed in the state of Illinois by a former employee. In November 2003, an ex-employee, Patrick Grant filed suit against Flexible Solutions in Cook County Circuit Court, Cook County IL, claiming wrongful dismissal and seeking return of options rights or cash. The company believes these allegations are without merit and intends to vigorously defend against them.
- b) The company is plaintiff in a lawsuit demanding return of the share certificate of 100,000 shares of stock originally given to the defendant as payment in advance for services. The services for which the advance was given were never performed or given to the company, and the company therefore received no consideration or value for such advance. Return of the share certificate for 100,000 shares was demanded within ten (10) days, namely August 22, 2001, however, to date remains unreturned.

On date of issue, January 4, 2001, the share transaction was recorded as shares issued for services at fair market value, a value of \$0.80 per share.

- c) The company has been named the defendant in a lawsuit filed in the Federal Court of Canada as well as the plaintiff in a countersuit in the same court. In July 2004, a former distributor, Sunsolar Energy Technologies, filed suit claiming trademark infringement. The company believes these allegations are without merit and intends to vigorously defend against them.

## **FLEXIBLE SOLUTIONS INTERNATIONAL INC.**

**Notes to Consolidated Financial Statements**

**Periods Ended September 30**

**(U.S. Dollars)**

**(Unaudited)**

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- d) The company is plaintiff in a lawsuit demanding the return of the share certificate of 100,000 shares of stock originally given as payment in advance for services, \$10,000 and undetermined damages resulting from a breach of contract. The suit has been filed in Circuit Court of Cook County, IL against Tatko Biotech Inc. of Peoria, IL. The services for which the advance was given were never performed or given to the company, and the company therefore received no consideration or value for such advance.

The shares issued were recorded at fair market value less 10%, resulting in an expense of \$271,000 recognized in June 2003.