

FLEXIBLE SOLUTIONS INTERNATIONAL INC  
Form 10-Q/A  
October 14, 2008

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

FORM 10-Q/A

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

For the quarterly period ended June 30, 2008

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 000-2969

FLEXIBLE SOLUTIONS INTERNATIONAL INC.  
(Exact Name of Issuer as Specified in Its Charter)

Nevada  
(State or other jurisdiction of  
incorporation or organization)

91-1922863  
(I.R.S. Employer Identification  
No.)

615 Discovery St.  
Victoria, British Columbia,  
Canada  
(Address of Issuer's Principal Executive  
Offices)

V8T 5G4  
(Zip Code)

Issuer's telephone number: (250) 477-9969

N/A

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

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) had been subject to such filing requirements for the past 90 days.

Yes        No

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Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check One):

Large accelerated filer [ ]

Accelerated filer [ ]

Non-accelerated filer [ ]

Smaller reporting company [X]

(Do not check if a smaller reporting company)

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

Yes            No    X

| Class of Stock | No. Shares Outstanding | Date            |
|----------------|------------------------|-----------------|
| Common         | 14,057,567             | October 1, 2008 |

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FORM 10-Q/A

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This document contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact are “forward-looking statements” for the purposes of the federal and state securities laws, including, but not limited to any projections of earnings, revenue or other financials items; any statements of the plans, strategies and objectives of management for future operations; any statements concerning proposed new services or developments; any statements regarding future economic conditions or performance; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing.

Forward-looking statements may include the words “may,” “could,” “will,” “estimate,” “intend,” “continue,” “believe,” “expect,” “anticipate” or other similar words. These forward-looking statements present our estimates and assumptions only as of the date of this report. Except for our ongoing obligation to disclose material information as required by the federal securities laws, we do not intend, and undertake no obligation, to update any forward-looking statement.

Although we believe that the expectations reflected in any of our forward-looking statements are reasonable, actual results could differ materially from those projected or assumed in any of our forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to change and inherent risks and uncertainties. The factors impacting these risks and uncertainties include but are not limited to:

- Increased competitive pressures from existing competitors and new entrants;
- Increases in interest rate or our cost of borrowing or a default under any material debt agreement;
- Deterioration in general or regional economic conditions;
- Adverse state or federal legislation or regulation that increases the costs of compliance, or adverse findings by a regulator with respect to existing operations;
- Loss of customers or sales weakness;
- Inability to achieve future sales levels or other operating results;
- The unavailability of funds for capital expenditures; and
- Operational inefficiencies in distribution or other systems.

For a detailed description of these and other factors that could cause actual results to differ materially from those expressed in any forward-looking statement, please see “Risk Factors” in our Annual Report on Form 10-KSB for the year ended December 31, 2007.

## PART I FINANCIAL INFORMATION

## Item Financial Statements.

1.

FLEXIBLE SOLUTIONS INTERNATIONAL, INC.  
CONSOLIDATED BALANCE SHEETS  
At June 30, 2008  
(U.S. Dollars)

|  | June 30,<br>2008<br>(Unaudited) | December<br>31,<br>2007 |
|--|---------------------------------|-------------------------|
| <b>Assets</b>  |                                 |                         |
| <b>Current</b>   |                                 |                         |
| Cash and cash equivalents                                  | \$ 1,107,960                    | \$ 3,355,854            |
| Accounts receivable  | 2,202,205                       | 1,051,056               |
| Inventory  | 2,914,164                       | 2,361,270               |
| Prepaid expenses   | 86,061                          | 115,353                 |
|  | 6,310,390                       | 6,883,533               |
| Property, equipment and leaseholds                         | 5,687,371                       | 4,612,571               |
| Patents  | 224,288                         | 230,438                 |
| Long term deposits   | 34,900                          | 48,034                  |
|  | \$ 12,256,949                   | \$ 11,774,576           |
| <b>Liabilities</b>   |                                 |                         |
| <b>Current</b>   |                                 |                         |
| Accounts payable and accrued liabilities                   | \$ 584,876                      | \$ 385,792              |
| Deferred revenue   | -                               | 9,870                   |
|  | 584,876                         | 395,662                 |
| Mortgage   | -                               | 452,018                 |
|  | \$ 584,876                      | \$ 847,680              |
| <b>Stockholders' Equity</b>                                |                                 |                         |
| <b>Capital stock</b>                                       |                                 |                         |
| <b>Authorized</b>  |                                 |                         |
| 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 |                                 |                         |
| <b>Issued and outstanding</b>                              |                                 |                         |
| 14,057,567 (2007: 14,057,567) common shares                | 14,058                          | 14,058                  |
| Capital in excess of par value                             | 16,079,694                      | 15,914,303              |
| Other comprehensive income                                 | 316,279                         | 394,289                 |
| Deficit  | (4,737,958)                     | (5,396,754)             |
| <b>Total Stockholders' Equity</b>                          | <b>11,672,073</b>               | <b>10,926,896</b>       |
| <b>Total Liabilities and Stockholders' Equity</b>          | <b>\$ 12,256,949</b>            | <b>\$ 11,774,576</b>    |

Commitments, Contingencies and Subsequent events (Notes 12, 13 &amp; 14)

-- See Notes to Unaudited Consolidated Financial Statements --



FLEXIBLE SOLUTIONS INTERNATIONAL, INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
For the Three Months Ended June 30, 2008 and 2007  
(U.S. Dollars -- Unaudited)

|   | Three Months Ended June |              |
|---|-------------------------|--------------|
|   | 2008                    | 2007         |
| Sales   | \$ 2,922,616            | \$ 2,143,107 |
| Cost of sales                                   | 1,648,373               | 1,260,324    |
| Gross profit                                    | 1,274,243               | 882,783      |
| Operating expenses                              |                         |              |
| Wages   | 322,029                 | 259,272      |
| Administrative salaries and benefits            | 80,885                  | 124,485      |
| Advertising and promotion                       | 28,780                  | 6,146        |
| Investor relations and transfer agent fee       | 42,191                  | 119,647      |
| Office and miscellaneous                        | 118,577                 | 65,578       |
| Insurance                                       | 53,049                  | 52,236       |
| Interest expense                                | (12,178)                | 159          |
| Rent  | 67,268                  | 56,738       |
| Consulting                                      | 37,661                  | 62,682       |
| Professional fees                               | 44,669                  | 42,477       |
| Travel  | 40,405                  | 48,287       |
| Telecommunications                              | 9,728                   | 9,845        |
| Shipping  | 10,913                  | 15,151       |
| Research  | 47,821                  | 22,974       |
| Commissions                                     | 52,445                  | 38,894       |
| Bad debt expense (recovery)                     | 362                     | 775          |
| Currency exchange                               | (16,682)                | 19,683       |
| Utilities                                       | 235                     | 4,439        |
|   | 928,157                 | 949,468      |
| Operating income (loss)                         | 346,086                 | (66,685)     |
| Other expenses                                  | -                       | (5,570)      |
| Interest income                                 | 1,537                   | 1,778        |
| Income (loss) before income tax                 | 347,623                 | (70,477)     |
| Net income (loss)                               | 347,623                 | (70,477)     |
| Net income (loss) per share (basic and diluted) | \$ 0.02                 | \$ (0.01)    |
| Weighted average number of common shares        | 14,057,567              | 13,841,489   |

-- See Notes to Unaudited Consolidated Financial Statements --



FLEXIBLE SOLUTIONS INTERNATIONAL, INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
For the Six Months Ended June 30, 2008 and 2007  
(U.S. Dollars -- Unaudited)

|   | Six Months Ended June 30, |              |
|---|---------------------------|--------------|
|   | 2008                      | 2007         |
| Sales   | \$ 6,421,089              | \$ 4,433,008 |
| Cost of sales                                   | 3,975,544                 | 2,726,675    |
| Gross profit                                    | 2,445,545                 | 1,706,333    |
| Operating expenses                              |                           |              |
| Wages   | 605,755                   | 516,458      |
| Administrative salaries and benefits            | 172,110                   | 256,282      |
| Advertising and promotion                       | 68,580                    | 38,024       |
| Investor relations and transfer agent fee       | 88,031                    | 177,838      |
| Office and miscellaneous                        | 191,275                   | 103,506      |
| Insurance                                       | 102,535                   | 107,065      |
| Interest expense                                | 1,963                     | 1,184        |
| Rent  | 135,110                   | 111,031      |
| Consulting                                      | 87,852                    | 127,679      |
| Professional fees                               | 66,407                    | 81,271       |
| Travel  | 68,019                    | 82,030       |
| Telecommunications                              | 18,929                    | 19,461       |
| Shipping  | 23,214                    | 23,244       |
| Research  | 67,782                    | 55,668       |
| Commissions                                     | 81,571                    | 75,597       |
| Bad debt expense (recovery)                     | 482                       | 1,851        |
| Currency exchange                               | (23,464)                  | 9,590        |
| Loss on sale of equipment                       | 29,048                    | -            |
| Utilities                                       | 4,577                     | 10,046       |
|   | 1,789,776                 | 1,797,825    |
| Operating income (loss)                         | 655,769                   | (91,492)     |
| Other expenses                                  | -                         | (5,570)      |
| Interest income                                 | 2,027                     | 2,371        |
| Income (loss) before income tax                 | 657,796                   | (94,691)     |
| Income tax (recovery)                           | -                         | -            |
| Net income (loss)                               | 657,796                   | (94,691)     |
| Net income (loss) per share (basic and diluted) | \$ 0.05                   | \$ (0.01)    |
| Weighted average number of common shares        | 14,057,567                | 13,485,482   |

-- See Notes to Unaudited Consolidated Financial Statements --

FLEXIBLE SOLUTIONS INTERNATIONAL, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
For the Six Months Ended June 30, 2008 and 2007  
(U.S. Dollars -- Unaudited)

|  | Six Months Ended June<br>30, |                     |
|--|------------------------------|---------------------|
|  | 2008                         | 2007                |
| <b>Operating activities</b>                              |                              |                     |
| Net income (loss)  | \$ 657,796                   | \$ (94,691)         |
| Stock compensation expense                               | 165,399                      | 278,976             |
| Depreciation   | 227,864                      | 256,206             |
|  | 1,051,059                    | 440,491             |
| <b>Changes in non-cash working capital items:</b>        |                              |                     |
| (Increase) Decrease in accounts receivable               | (1,151,149)                  | (56,621)            |
| (Increase) Decrease in inventory                         | (552,894)                    | (12,207)            |
| (Increase) Decrease in prepaid expenses                  | 29,292                       | (12,280)            |
| Increase (Decrease) in accounts payable                  | 199,084                      | (117,472)           |
| Increase (Decrease) in deferred revenue                  | 9,870                        | (20,559)            |
| <b>Cash provided by (used in) operating activities</b>   | <b>(434,478)</b>             | <b>221,353</b>      |
| <b>Investing activities</b>                              |                              |                     |
| Long term deposits                                       | 13,134                       | (1,408)             |
| Development of patents                                   | 6,150                        | (34,772)            |
| Acquisition of property and equipment                    | (1,754,682)                  | (20,390)            |
| <b>Cash provided by (used in) investing activities</b>   | <b>(1,735,398)</b>           | <b>(56,570)</b>     |
| <b>Financing activities</b>                              |                              |                     |
| Proceeds from issuance of common stock                   | -                            | 3,164,481           |
| <b>Cash provided by financing activities</b>             | <b>-</b>                     | <b>3,164,481</b>    |
| <b>Effect of exchange rate changes on cash</b>           | <b>(78,018)</b>              | <b>133,072</b>      |
| <b>Inflow (outflow) of cash</b>                          | <b>(2,247,894)</b>           | <b>3,462,336</b>    |
| Cash and cash equivalents, beginning                     | 3,335,854                    | 450,759             |
| <b>Cash and cash equivalents, ending</b>                 | <b>\$ 1,107,960</b>          | <b>\$ 3,913,094</b> |
| <b>Supplemental disclosure of cash flow information:</b> |                              |                     |
| Interest paid  | \$ 1,963                     | \$ 1,184            |

-- See Notes to Unaudited Consolidated Financial Statements --

FLEXIBLE SOLUTIONS INTERNATIONAL, INC.  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
For the Period Ended June 30, 2008  
(U.S. Dollars)

1. Basis of Presentation.

These unaudited consolidated financial statements of Flexible Solutions International, Inc (the “Company”) have been prepared in accordance with accounting principles generally accepted 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, 2007 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 June 30, 2008, and the consolidated results of operations and the consolidated statements of cash flows for the six months ended June 30, 2008 and 2007. The results of operations for the six months ended June 30, 2008 are not necessarily indicative of the results to be expected for the entire fiscal year.

These consolidated financial statements include the accounts of Flexible Solutions International, Inc. (the “Company”), and its wholly-owned subsidiaries Flexible Solutions, Ltd. (“Flexible Ltd.”), NanoChem Solutions Inc., WaterSavr Global Solutions Inc., NanoDetect Technologies Inc. and Seahorse Systems Inc. All inter-company balances and transactions have been eliminated. The Company was incorporated May 12, 1998 in Nevada and had no operations until June 30, 1998.

Flexible Solutions International, Inc. and its subsidiaries develop, manufactures and markets specialty chemicals which slow down the evaporation of water. The Company’s primary product, HEAT\$AVR®, is marketed for use in swimming pools and spas where its use, by slowing the evaporation of water, allows the water to retain a higher temperature for a longer period of time and thereby reduces the energy required to maintain the desired temperature of the water in the pool. Another product, WATER\$AVR®, is marketed for water conservation in irrigation canals, aquaculture, and reservoirs where its use slows down water loss due to evaporation. In addition to the water conservation products, the Company also manufacturers and markets water-soluble chemicals utilizing thermal polyaspartate biopolymers (referred to as “TPAs”), which are beta-proteins manufactured from the common biological amino acid, L-aspartic. TPAs can be formulated to prevent corrosion and scaling in water piping within the petroleum, chemical, utility and mining industries. TPAs are also used as proteins to enhance fertilizers in improving crop yields and as additives for household laundry detergents, consumer care products and pesticides.

On May 2, 2002, the Company formed WaterSavr Global Solutions Inc.

On February 7, 2005, the Company formed Nano Detect Technologies Inc.

On June 21, 2005, the Company formed Seahorse Systems Inc.

Pursuant to a purchase agreement dated May 26, 2004, the Company acquired the assets of Donlar Corporation (“Donlar”) on June 9, 2004 and created a new company, NanoChem Solutions Inc. as the operating entity for such assets. 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 4% to Donlar’s largest creditor to satisfy \$3,150,000 of the purchase price. This note was paid June 2, 2005 and upon payment, all former Donlar assets that were pledged as security were released from their mortgage. The

remainder of the consideration given was cash.

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The following table summarizes the estimated fair value of the assets acquired at the date of acquisition (at June 9, 2004):

|  |              |
|--|--------------|
| Current assets                                       | \$ 1,126,805 |
| Property and equipment                               | 5,023,195    |
|  | \$ 6,150,000 |
| Acquisition costs assigned to property and equipment | 314,724      |
| Total assets acquired                                | \$ 6,464,724 |

There was no goodwill or other intangible assets except certain patents recorded at nil fair value, acquired as a result of the acquisition. The acquisition costs assigned to property and equipment include all direct costs incurred by the Company to purchase the Donlar assets. These costs include due diligence fees paid to outside parties investigating and identifying the assets, legal costs directly attributable to the purchase of the assets, plus applicable transfer taxes. These costs have been assigned to the individual assets based on their proportional fair values and will be amortized based on the rates associated with the related assets.

## 2. Significant Accounting Policies.

These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States 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) Inventories and Cost of Sales

The Company has three major classes of inventory: finished goods, works in progress, raw materials and supplies. In all classes, inventory is valued at the lower of cost and market. Cost is determined on a first-in, first-out basis. Cost of sales includes all expenditures incurred in bringing the goods to the point of sale. Inventory costs and costs of sales include direct costs of the raw material, inbound freight charges, warehousing costs, handling costs (receiving and purchasing) and utilities and overhead expenses related to the Company's manufacturing and processing facilities.

In 2004, the FASB issued SFAS No. 151, "Inventory Costs", to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs and wasted material. This standard requires that such items be recognized as current-period charges. The standard also establishes the concept of "normal capacity" and requires the allocation of fixed production overhead to inventory based on the normal capacity of the production facilities. Any unallocated overhead must be recognized as an expense in the period incurred. This standard is effective for inventory costs incurred starting January 1, 2006. The adoption of this standard did not have a material impact on the Company's financial position, results of operations or cash flows for 2007 or 2008.

## (c) Allowance for Doubtful Accounts

The Company provides an allowance for doubtful accounts when management estimates collectibility is uncertain. Accounts receivable are continually reviewed to determine which, if any, accounts are doubtful of collection. In making the determination of the appropriate allowance amount, the Company considers current economic and industry conditions, relationships with each significant customer, overall customer credit-worthiness and historical experience.

## (d) Property, Equipment and Leaseholds.

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

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

Depreciation is recorded at half for the year the assets are first purchased. 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.

## (e) Impairment of Long-Lived Assets.

In accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", the Company reviews long-lived assets, including, but not limited to, property and equipment, patents and other assets, for impairment annually or whenever events or changes in circumstances indicate the carrying amounts of assets may not be recoverable. The carrying value of long-lived assets is assessed for impairment by evaluating operating performance and future undiscounted cash flows of the underlying assets. If the sum of the expected future cash flows of an asset, is less than its carrying value, an impairment measurement is indicated. Impairment charges are recorded to the extent that an asset's carrying value exceeds its fair value. Accordingly, actual results could vary significantly from such estimates. There were no impairment charges during the periods presented.

## (f) Investments.

Investment in corporations subject to significant influence and investments in partnerships are recorded using the equity method of accounting. On this basis, the Company's share of income and losses of the corporations and partnerships is included in earnings and the Company's investment therein adjusted by a like amount. Dividends received from these entities reduce the investment accounts. Portfolio investments not subject to significant influence are recorded using the cost method.

The fair value of a cost method investment is not estimated if there are no identified events or changes in circumstances that may have a significant adverse effect on the fair value of the investment.

The Company currently does not have any investments that require use of the equity method of accounting.



(g) Foreign Currency.

The functional currency of one of the subsidiaries 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 loss and are 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 the operating loss if realized during the year and in comprehensive income if they remain unrealized at the end of the year.

(h) Revenue Recognition.

Revenue from product sales is recognized at the time the product is shipped since title and risk of loss is transferred to the purchaser upon delivery to the carrier. Shipments are made F.O.B. shipping point. The Company recognizes revenue when there is persuasive evidence of an arrangement, delivery has occurred, the fee is fixed or determinable, collectibility is reasonably assured and there are no significant remaining performance obligations. When significant post-delivery obligations exist, revenue is deferred until such obligations are fulfilled. To date there have been no such significant post-delivery obligations.

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.

(i) Stock Issued in Exchange for Services.

The valuation of the Company's 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. The corresponding expense of the services rendered is recognized over the period that the services are performed.

(j) Stock-based Compensation.

In December 2004, the Financial Accounting Standards Board ("FASB") issued revised SFAS No. 123(R), Share-Based Payment, which replaces SFAS No. 123, "Accounting for Stock-Based Compensation", which superseded APB Opinion No. 25, "Accounting for Stock Issued to Employees". FAS No. 123(R) requires the cost of all share-based payment transactions to be recognized in an entity's financial statements, establishes fair value as the measurement objective and requires entities to apply a fair-value-based measurement method in accounting for share-based payment transactions. SFAS No. 123(R) applies to all awards granted, modified, repurchased or cancelled after July 1, 2005, and unvested portions of previously issued and outstanding awards. The Company adopted this statement for its first quarter starting January 1, 2006 and will continue to evaluate the impact of adopting this statement.

Prior to 2006, the Company adopted the disclosure provisions of SFAS No. 123 for stock options granted to employees and directors. The Company disclosed on a supplemental basis, the pro-forma effect of accounting for stock options awarded to employees and directors, as if the fair value based method had been applied, using the Black-Scholes option-pricing model. The Company has always recognized the fair value of options granted to consultants.





(k) 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.

(l) Income (Loss) Per Share.

Income (loss) per share is calculated by dividing net income (loss) by the weighted average number of shares outstanding. Diluted loss per share is computed by giving effect to all potential dilutive options that were outstanding during the year. For the periods ended June 30, 2008 and 2007, all outstanding options were anti-dilutive.

(m) Use of Estimates.

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States 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.

(n) 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 maintains cash balances at financial institutions which at times, exceed federally insured amounts. The Company has not experienced any material losses in such accounts.

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.

The Company is exposed to credit-related losses in the event of non-performance by counterparties to the financial instruments. Credit exposure is minimized by dealing with only credit worthy counterparties. Accounts receivable for the three primary customers totals \$1,428,166 (65%) as at June 30, 2008 (2007 - \$466,031 or 64%).

(o) Contingencies

Certain conditions may exist as of the date the financial statements are issued, which may result in a loss to the Company but which will only be resolved when one or more future events occur or fail to occur. The Company's management and its legal counsel assess such contingent liabilities, and such assessment inherently involves an exercise of judgment. In assessing loss contingencies related to legal proceedings that are pending against the Company or unasserted claims that may result in such proceedings, the Company's legal counsel evaluates the perceived merits of any legal proceedings or unasserted claims as well as the perceived merits of the amount of relief sought or expected to be sought therein.

If the assessment of a contingency indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, the estimated liability would be accrued in the Company's financial statements. If the assessment indicates that a potentially material loss contingency is not probable but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability, together with an estimate of the range of

possible loss if determinable and material, would be disclosed.

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Loss contingencies considered remote are generally not disclosed unless they involve guarantees, in which case the guarantees would be disclosed.

(p) Recent Accounting Pronouncements

Business Combinations

In December 2007, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards (“FAS”) No. 141 (Revised 2007), “Business Combinations” (“FAS 141(R”). FAS 141(R) establishes principles and requirements for how an acquirer in a business combination recognizes and measures in its financial statements the identifiable assets acquired, liabilities assumed, and any noncontrolling interests in the acquiree, as well as the goodwill acquired. Significant changes from current practice resulting from FAS 141(R) include the expansion of the definitions of a “business” and a “business combination.” For all business combinations (whether partial, full or step acquisitions), the acquirer will record 100% of all assets and liabilities of the acquired business, including goodwill, generally at their fair values; contingent consideration will be recognized at its fair value on the acquisition date and, for certain arrangements, changes in fair value will be recognized in earnings until settlement; and acquisition-related transaction and restructuring costs will be expensed rather than treated as part of the cost of the acquisition. FAS 141(R) also establishes disclosure requirements to enable users to evaluate the nature and financial effects of the business combination. FAS 141(R) applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. Earlier adoption is not permitted. The Company is currently evaluating the potential impact of this statement.

Noncontrolling Interests in Consolidated Financial Statements

In December 2007, the FASB issued FAS No. 160, “Noncontrolling Interests in Consolidated Financial Statements — An amendment of ARB No. 51” (“FAS 160”). FAS 160 amends Accounting Research Bulletin 51, “Consolidated Financial Statements,” to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. It clarifies that a noncontrolling interest in a subsidiary, which is sometimes referred to as minority interest, is a third-party ownership interest in the consolidated entity that should be reported as a component of equity in the consolidated financial statements. Among other requirements, FAS 160 requires the consolidated statement of income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest. FAS 160 also requires disclosure on the face of the consolidated statement of income of the amounts of consolidated net income attributable to the parent and to the noncontrolling interest. FAS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. Earlier adoption is not permitted. The Company is currently evaluating the potential impact of this statement.

Fair Value Measurements

In February 2008, the FASB issued FASB Staff Position No. FAS 157-2, “Effective Date of FASB Statement No. 157” (“FSP 157-2”), to partially defer FASB Statement No. 157, “Fair Value Measurements” (“FAS 157”). FSP 157-2 defers the effective date of FAS 157 for nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), to fiscal years, and interim periods within those fiscal years, beginning after November 15, 2008. The Company is currently evaluating the impact of adopting the provisions of FAS 157 as it relates to non-financial assets and liabilities.

## Disclosures about Derivative Instruments and Hedging Activities

In March 2008, the FASB issued FAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities" ("FAS 161"). FAS 161 amends and expands the disclosure requirements of FAS 133, "Accounting for Derivative Instruments and Hedging Activities" and requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. This statement is effective for financial statements issued for fiscal periods beginning after November 15, 2008. Earlier adoption is not permitted. The Company does not believe the adoption of FAS 161 will have a material impact on its consolidated financial statements.

## Determination of Useful Life of Intangible Assets

In April 2008, the FASB issued FASB Staff Position ("FSP") FAS 142-3, "Determination of Useful Life of Intangible Assets" ("FSP FAS 142-3"). FSP FAS 142-3 amends the factors that should be considered in developing the renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FAS 142, "Goodwill and Other Intangible Assets." FSP FAS 142-3 also requires expanded disclosure related to the determination of intangible asset useful lives. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008. Earlier adoption is not permitted. The Company is currently evaluating the potential impact the adoption of FAS FSP 142-3 will have on its consolidated financial statements.

## 3. Inventories

|                   | 2008         | 2007         |
|-------------------|--------------|--------------|
| Completed goods   | \$ 1,184,858 | \$ 1,664,777 |
| Works in progress | 347,099      | 198,172      |
| Raw materials     | 1,382,207    | 498,321      |
|                   | \$ 2,914,164 | \$ 2,361,270 |

## 4. Property, Plant &amp; equipment

|                         | 2008<br>Cost | Accumulated<br>Depreciation | 2008<br>Net  |
|-------------------------|--------------|-----------------------------|--------------|
| Buildings               | \$ 4,181,583 | \$ 1,079,085                | \$ 3,102,498 |
| Building Improvements   | 352,297      | —                           | 352,297      |
| Computer hardware       | 79,902       | 52,062                      | 27,840       |
| Furniture and fixtures  | 21,621       | 12,861                      | 8,761        |
| Office equipment        | 32,277       | 22,682                      | 9,595        |
| Manufacturing equipment | 2,880,631    | 1,345,448                   | 1,535,183    |
| Trailer                 | 27,571       | 5,675                       | 21,896       |
| Leasehold improvements  | 28,117       | 21,750                      | 6,367        |
| Technology              | 139,152      | -                           | 139,152      |
| Trade show booth        | 8,522        | 6,412                       | 2,110        |
| Truck                   | 11,660       | 1,749                       | 9,911        |
| Land                    | 471,761      | —                           | 471,761      |
|                         | \$ 8,235,094 | \$ 2,547,723                | \$ 5,687,371 |

|                         | 2007<br>Cost | Accumulated<br>Depreciation | 2007<br>Net  |
|-------------------------|--------------|-----------------------------|--------------|
| Buildings               | \$ 4,011,826 | \$ 970,854                  | \$ 3,040,972 |
| Computer hardware       | 75,458       | 48,284                      | 27,174       |
| Furniture and fixtures  | 21,788       | 12,154                      | 9,634        |
| Office equipment        | 32,905       | 22,035                      | 10,870       |
| Manufacturing equipment | 2,313,363    | 1,280,943                   | 1,032,420    |
| Trailer                 | 3,854        | 1,863                       | 1,990        |
| Leasehold improvements  | 46,304       | 36,480                      | 9,825        |
| Trade show booth        | 8,766        | 6,212                       | 2,554        |
| Land                    | 477,133      | —                           | 477,133      |
|                         | \$ 6,991,397 | \$ 2,378,829                | \$ 4,612,571 |

#### 5. Patents

In fiscal 2005, the Company started the patent process for additional WATER\$AVR® products. Patents associated with these costs were granted in 2006 and they have been amortized over their legal life of 17 years.

Of the patents costs listed below, \$72,786 are not subject to amortization as of yet, as the patents are still in the process of being approved.

|         | 2008<br>Cost | Accumulated<br>Amortization | 2008<br>Net |
|---------|--------------|-----------------------------|-------------|
| Patents | \$ 239,061   | \$ 14,773                   | \$ 224,288  |

|         | 2007<br>Cost | Accumulated<br>Amortization | 2007<br>Net |
|---------|--------------|-----------------------------|-------------|
| Patents | \$ 243,853   | \$ 13,415                   | \$ 230,438  |

#### 6. Long Term Deposits

The Company has reclassified certain security deposits to better reflect their long term nature. Long term deposits consist of damage deposits held by landlords and security deposits held by various vendors.

|                    | 2008      | 2007      |
|--------------------|-----------|-----------|
| Long term deposits | \$ 34,900 | \$ 48,034 |

#### 7. Stock Options

The Company adopted a stock option plan ("Plan"). The purpose of this Plan is to provide additional incentives to key employees, officers, directors and consultants of the Company and its subsidiaries in order to help attract and retain the best available personnel for positions of responsibility and otherwise promoting the success of the business activities. It is intended that options issued under this Plan constitute non-qualified stock options. The general terms of awards under the option plan are that 100% of the options granted will vest the year following the grant. The maximum term of options granted is 5 years.



The Company may issue stock options and stock bonuses for shares of its common stock to provide incentives to directors, key employees and other persons who contribute to the success of the Company. The exercise price of all incentive options are issued for not less than fair market value at the date of grant.

The following table summarizes the Company's stock option activity for the years ended December 31, 2006, 2007 and the period ended June 30, 2008:

|                            | Number of shares | Exercise price per share | Weighted average exercise price |
|----------------------------|------------------|--------------------------|---------------------------------|
| Balance, December 31, 2005 | 1,060,740        | \$ 1.40 - \$4.60         | \$ 3.44                         |
| Granted                    | 1,191,000        | \$ 3.25 - \$3.60         | \$ 3.25                         |
| Exercised                  | (46,000)         | \$ 1.40                  | \$ 1.40                         |
| Cancelled or expired       | (79,000)         | \$ 1.40 - \$4.25         | \$ 2.46                         |
| Balance, December 31, 2006 | 2,126,740        | \$ 1.40 - \$4.60         | \$ 3.44                         |
| Granted                    | 235,700          | \$ 1.50 - \$3.60         | \$ 2.35                         |
| Exercised                  | (163,000)        | \$ 1.50 - \$3.25         | \$ 1.77                         |
| Cancelled or expired       | (287,000)        | \$ 3.00 - \$4.40         | \$ 3.93                         |
| Balance, December 31, 2007 | 1,912,440        | \$ 3.00 - \$4.60         | \$ 3.38                         |
| Granted                    | 83,000           | \$ 3.00 - \$3.60         | \$ 3.60                         |
| Balance, June 30, 2008     | 1,995,440        | \$ 3.00 - \$4.55         | \$ 3.39                         |

The fair value of each option grant is calculated using the following weighted average assumptions:

|  | 2008    | 2007           |
|--|---------|----------------|
| Expected life – years                          | 5.0     | 1.0 - 5.0      |
| Interest rate                                  | 2.27%   | 4.18 - 5.18%   |
| Volatility                                     | 99%     | 86.0 - 115.0%  |
| Dividend yield                                 | —%      | —%             |
| Weighted average fair value of options granted | \$ 1.15 | \$ 1.37 - 2.67 |

During the six months ended June 30, 2008 the Company granted 46,000 options to consultants that resulted in \$26,478 in expenses this period. During the same period, 37,000 options were granted to employees, resulting in \$21,298 in expenses this period. Options granted in previous quarters resulted in additional expenses in the amount of \$40,850 for consultants and \$76,773 for employees during the six months ended June 30, 2008. No stock options were exercised during the period.

During the six months ended June 30, 2007, the Company granted 150,000 stock options to a third party as a part of the litigation settlement made January 3, 2007. As the options were previously granted and expensed in 2001, no



expense was recorded in this period related to this transaction. During the same period, the Company granted 50,700 options to consultants and has applied FAS No. 123(R) using the Black-Scholes option-pricing model, which resulted in additional expenses of \$29,130 during the three months ended June 30, 2007. Options granted in previous quarters but not yet vested realized expenses of \$94,128 for third parties and \$155,718 for employees for the six months ended June 30, 2007.

8. Warrants

On April 14, 2005, the Company announced that it had raised \$3,375,000 pursuant to a private placement of up to 1,800,000 shares of its common stock. The investors collectively purchased 900,000 shares of the Company's common stock at a per share purchase price of \$3.75, together with warrants to purchase up to 900,000 additional shares of the Company's common stock. The warrants have a four-year term and are exercisable at a price of \$4.50 per share.

On June 8, 2005, the Company announced that it had raised an additional \$327,750 pursuant to a private placement. An investor purchased 87,400 shares of the Company's common stock at a per share price of \$3.75, together with a warrant to purchase up to 87,400 additional shares of the Company's common stock. The warrant has a four-year term and is immediately exercisable at a price of \$4.50 per share.

In May 2007 the Company closed a \$3,042,455 private placement with institutional investors. The terms are 936,140 units with each unit consisting of one share at \$3.25 and one half warrant with a three year term and a strike price of \$4.50 per share. The Company also issued 21,970 warrants with the same terms for investment banking services related to this transaction.

The following table summarizes the Company's warrant option activity for the three years ended December 30, 2007 (no subsequent activity):

|                            | Number of<br>shares | Exercise<br>price<br>per share | Weighted<br>average<br>exercise<br>price |
|----------------------------|---------------------|--------------------------------|--|
| Balance, December 31, 2004 | —                   | —                              | —  |
| Granted                    | 987,400             | \$ 4.50                        | \$ 4.50                                  |
| Exercised                  | —                   | —                              | —  |
| Cancelled                  | —                   | —                              | —  |
| Balance, December 31, 2005 | 987,400             | \$ 4.50                        | \$ 4.50                                  |
| Granted                    | —                   | —                              | —  |
| Exercised                  | —                   | —                              | —  |
| Cancelled                  | —                   | —                              | —  |
| Balance, December 31, 2006 | 987,400             | \$ 4.50                        | \$ 4.50                                  |
| Granted                    | 490,040             | \$ 4.50                        | \$ 4.50                                  |
| Exercised                  | —                   | —                              | —  |
| Cancelled                  | —                   | —                              | —  |
| Balance, December 30, 2007 | 1,477,440           | \$ 4.50                        | \$ 4.50                                  |

#### 9. Capital Stock.

During the six months ended June 30, 2007, the Company issued 200,700 shares of common stock upon the exercise of stock options. The strike price varied from \$1.50 – 3.25 per share.

In May 2007 the Company closed a \$3,042,455 private placement with institutional investors. The terms are 936,140 units with each unit consisting of one share at \$3.25 and one half warrant with a three year term and a strike price of \$4.50 per share. The proceeds will be used to build a biomass conversion facility that will use renewable agriculture crops to produce aspartic acid.

No stock was issued during the six months ended June 30, 2008.

#### 10. Segmented, Significant Customer Information and Economic Dependency.

The Company operates in two segments:

(a) Development and marketing of two lines of energy and water conservation products (as shown under the column heading "EWCP" below), which consists of a (i) liquid swimming pool blanket which saves energy and water by inhibiting evaporation from the pool surface, and (ii) food-safe powdered form of the active ingredient within the

liquid blanket and which is designed to be used in still or slow moving drinking water sources.

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(b) Manufacture of biodegradable polymers and chemical additives used within the petroleum, chemical, utility and mining industries to prevent corrosion and scaling in water piping (as shown under the column heading "BPCA" below). These chemical additives are also manufactured for use in laundry and dish detergents, as well as in products to reduce levels of insecticides, herbicides and fungicides.

The Company's traditional operating activities related to the production and sale of its energy conversation product line. Upon acquiring the Donlar assets, the Company formed NanoChem, which was formed as its wholly-owned subsidiary in exchange for the capital contribution necessary to purchase the Donlar assets. The assets the Company acquired from Donlar include domestic and international patents and business processes relating to the production of TPAs and other environmental products and technologies, as well as a manufacturing plant. These assets are currently used by NanoChem for its revenue-producing activities.

The accounting policies of the segments are the same as those described in Note 2, Significant Accounting Policies. The Company evaluates performance based on profit or loss from operations before income taxes, not including nonrecurring gains and losses and foreign exchange gains and losses.

The Company's reportable segments are strategic business units that offer different, but synergistic products and services. They are managed separately because each business requires different technology and marketing strategies.

Six months ended June 30, 2008:

|                                 | EWCP       | BPCA         | Total        |
|---------------------------------|------------|--------------|--------------|
| Revenue                         | \$ 792,640 | \$ 5,628,449 | \$ 6,421,089 |
| Interest revenue                | 1,318      | 709          | 2,027        |
| Interest expense                | 382        | 1,581        | 1,963        |
| Depreciation and amortization   | 27,208     | 200,656      | 227,864      |
| Segment profit (loss)           | (641,006)  | 1,298,802    | 657,796      |
| Segment assets                  | 2,582,140  | 3,105,231    | 5,687,371    |
| Expenditures for segment assets | 1,720,270  | 34,128       | 1,754,398    |

Six months ended June 30, 2007:

|                                 | EWCP       | BPCA         | Total        |
|---------------------------------|------------|--------------|--------------|
| Revenue                         | \$ 998,289 | \$ 3,434,719 | \$ 4,433,008 |
| Interest revenue                | 1,517      | 854          | 2,371        |
| Interest expense                | 523        | 661          | 1,184        |
| Depreciation and amortization   | 26,256     | 229,950      | 256,206      |
| Segment profit (loss)           | 633,516    | 538,825      | (94,691)     |
| Segment assets                  | 193,507    | 3,671,230    | 3,864,737    |
| Expenditures for segment assets | 20,153     | 237          | 20,390       |

The sales generated in the United States and Canada are as follows:

|                          | 2008         | 2007         |
|--------------------------|--------------|--------------|
| Canada                   | \$ 187,983   | \$ 58,587    |
| United States and abroad | 6,233,106    | 4,374,421    |
| Total                    | \$ 6,421,089 | \$ 4,433,008 |

The Company's long-lived assets are located in Canada and the United States as follows:

|               | 2008         | 2007         |
|---------------|--------------|--------------|
| Canada        | \$ 2,803,003 | \$ 1,331,166 |
| United States | 3,108,656    | 3,511,843    |
| Total         | \$ 5,911,659 | \$ 4,843,009 |

Three customers account for \$3,158,923 (49%) of sales made in the period (2007 - \$1,799,725 or 41%).

#### 11. Commitments.

The Company is committed to minimum rental payments for property and premises aggregating approximately \$252,347 over the term of four leases, the last expiring on December 31, 2011.

Commitments in each of the next five years are approximately as follows:

|      |           |
|------|-----------|
| 2008 | \$ 91,380 |
| 2009 | 128,011   |
| 2010 | 16,478    |
| 2011 | 16,478    |
| 2012 | -         |

#### 12. Contingencies.

On May 1, 2003, the Company filed a lawsuit in the Supreme Court of British Columbia, Canada, against John Wells and Equity Trust, S.A. seeking the return of 100,000 shares of the Company's common stock and the repayment of a \$25,000 loan, which were provided to defendants for investment banking services consisting of securing a \$5 million loan and a \$25 million stock offering. Such services were not performed and in the proceeding the Company seeks return of such shares after defendant's failure to both return the shares voluntarily and repay the note. On May 7, 2003, the Company obtained an injunction freezing the transfer of the shares. On May 24, 2004, there was a hearing on defendant's motion to set aside the injunction, which motion was denied by the trial court on May 29, 2004. On the date of issuance, the share transaction was recorded as shares issued for services at fair market value, a value of \$0.80 per share. No amounts have been recorded as receivable in the Company's consolidated financial statements as the outcome of this claim is not determinable.

As of January 3, 2007 all litigation between the Company and Patrick Grant has been settled. As part of the settlement the Company permitted Mr. Grant to exercise an option to purchase 100,000 shares of the Company's common stock at a price of \$1.50 per share and to exercise a second option to purchase 50,000 shares of the Company's common stock at a price of \$2.00 per share. The Company also forgave a loan to Mr. Grant and related parties in the amount of approximately \$46,177. This amount has been recorded as a bad debt expense in 2006. The Company, its subsidiaries and officers face no further liability in regard to the Grant lawsuit.



On July 23, 2004, the Company filed a lawsuit in the Circuit Court of Cook County, Illinois against Tatko Biotech Inc. ("Tatko"). The action arose from a Joint Product Development Agreement with Tatko in which the Company agreed to invest \$10,000 toward the product development venture and granted to Tatko 100,000 shares of the Company's restricted common stock. In return, Tatko granted us a five-year option to purchase 20% of Tatko's outstanding capital stock. Tatko refused to collaborate on the agreement and, therefore, the Company filed the lawsuit to have the court declare that Tatko is not entitled to the 100,000 shares of the Company's restricted common stock. On January 4, 2008, the lawsuit was dismissed pursuant to an agreement by Tatko to treat the Joint Product Development Agreement as void. As a result of the dismissal of the lawsuit and the agreement of the parties, the 100,000 shares of restricted stock will be returned or cancelled.

13. Subsequent Events.

There have been no subsequent events.

14. Comparative Figures.

Certain of the comparative figures have been reclassified to conform with the current year's presentation.

## Item Management's Discussion and Analysis or Plan of Operation.

2.

## Overview

Flexible Solutions International, Inc. ("we," "us," and "our") develops, manufactures and markets specialty chemicals that slow the evaporation of water. Our initial product, HEAT\$AVR®, is marketed for use in swimming pools and spas where its use, by slowing the evaporation of water, allows the water to retain a higher temperature for a longer period of time and thereby reduces the energy required to maintain the desired temperature of the water in the pool. Using the same technology, WATER\$AVR®, is marketed for water conservation in irrigation canals, aquaculture, and reservoirs where its use slows water loss due to evaporation. We also manufacture and market TPA's for use in the oilfields to reduce scale and corrosion in many 'topside' water systems and in the agriculture industry to reduce fertilizer crystallization before, during and after application.

## Results of Operations

The Company has two product lines:

The first is a chemical ("EWCP") used in swimming pools and spas. The product forms a thin, transparent layer on the water's surface. The transparent layer slows the evaporation of water, allowing the water to retain a higher temperature for a longer period of time and thereby reducing the energy required to maintain the desired temperature of the water. A modified version of the product can also be used in reservoirs, potable water storage tanks, livestock watering ponds, canals, and irrigation ditches.

The second product ("BPCA") combines biodegradable polymers and chemical additives and is used by the petroleum, chemical, utility and mining industries to prevent corrosion and scaling in water piping. This product can also be used in detergent to increase biodegradability and in agriculture to increase crop yields by enhancing fertilizer uptake.

Material changes in our Statement of Operations for the periods presented are discussed below:

## Six Months Ended June 30, 2008

| Item                                 | Increase (I) or<br>Decrease (D) | Reason   |
|--------------------------------------|---------------------------------|--|
| Sales:<br>EWCP products              | D                               | During the six months ended June 30, 2008 a drought in Australia eased, which reduced sales of energy and water conservation products. In addition, energy and water conservation products for use in swimming pools decreased due to real estate foreclosures in the United States. |
| BPCA products                        | I                               | Maintenance shutdowns in the oil extraction industry during 2007.reduced sales during the six months ended June 30, 2007.  |
| Wages                                | I                               | Increased sales required increased support on all levels.  |
| Administrative salaries and benefits | D                               | Five year stock option plans granted to several long term employees in 2006 resulted in higher expenses in 2007. Granting of stock options resulted in an expense of \$102,301 in first six months of 2007 as compared to \$62,443 in the same period 2008.                          |



|   |   |   |
|---|---|---|
| Investor relations and transfer agent fee | D | Options granted in relation to the private placement in May 2007 increased our investor relations costs during that period.   |
| Office and miscellaneous                  | I | Various administrative costs associated with the start up of the new facility have been allocated to this account. Once the facility is operational, these costs will be allocated to overhead.     |
| Consulting                                | D | The granting of stock options to long term consultants in 2006 resulted in a stock option expense of \$40,851 in the six month ended June 30, 2008 as compared to \$65,609 in the same period 2007. |

Three Months Ended June 30, 2008

|   |   |  |
|---|---|--|
| Sales:<br>EWCP products                   | D | During the three months ended June 30, 2008 a drought in Australia eased, which reduced sales of energy and water conservation products. In addition, energy and water conservation products for use in swimming pools decreased due to real estate foreclosures in the United States. |
| BPCA products                             | I | Maintenance shutdowns in the oil extraction industry during 2007 reduced sales during the three months ended June 30, 2007.  |
| Wages                                     | I | Increased sales required increased support on all levels.  |
| Administrative salaries and benefits      | D | Five year stock option plans granted to several long term employees in 2006 resulted in higher expenses in 2007 than 2008. Granting of stock options plans resulted in an expense of \$51,150 in second quarter 2007 as compared to \$31,222 in the same period 2008.                  |
| Investor relations and transfer agent fee | D | Options granted in relation to the private placement in May 2007 increased our investor relations costs during that period.  |
| Office and miscellaneous                  | I | Various administrative costs associated with the start up of the new facility have been allocated to this account. Once the facility is operational, these costs will be allocated to overhead.  |
| Consulting                                | D | The granting of stock options to long-term consultants in 2006 resulted in a stock option expense of \$14,590 in first quarter 2008 as compared to \$32,805 in the same period 2007.   |
| Commissions                               | I | Increased sales for the quarter resulted in increased commissions.   |

#### Capital Resources and Liquidity

The sources and uses of funds are directly obtainable from the Consolidated Statement of Cash Flows included as part of the financial statements filed with this report.

The Company has sufficient cash resources to meet its future commitments and cash flow requirements for the coming year. As of June 30, 2008 working capital was \$5,725,514 (2007 - \$7,036,894) and the Company has no

substantial commitments that require significant outlays of cash over the coming fiscal year.

The Company is committed to minimum rental payments for property and premises aggregating approximately \$252,347 over the term of four leases, the last expiring on December 31, 2011.

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Commitments in each of the next five years are approximately as follows:

|      |    |         |
|------|----|---------|
| 2008 | \$ | 91,380  |
| 2009 |    | 128,011 |
| 2010 |    | 16,478  |
| 2011 |    | 16,478  |
| 2012 |    | -       |

The Company doesn't anticipate any capital requirements for the twelve months ending December 31, 2008.

The Company does not have any commitments or arrangements from any person to provide with any additional capital.

See Note 2 to the financial statements included as part of this report for a description of our significant accounting policies and recent accounting pronouncements.

ItemControls and Procedures.

4T.

Daniel O'Brien, Flexible Solution International Inc.'s Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report; and in his opinion the Company's disclosure controls and procedures were effective. There were no changes in the Company's internal controls over financial reporting that occurred during the quarter ended June 30, 2008 that have affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

#### Management's Report on Internal Control Over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting as required by Sarbanes-Oxley (SOX) Section 404.A. The Company's internal control over financial reporting is a process designed under the supervision of its Chief Executive and Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of their financial statements for external purposes in accordance with Generally Accepted Accounting Principles.

As of the end of the period covered by this report, the Company's management assessed the effectiveness of its internal control over financial reporting based on the criteria for effective internal control over financial reporting established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") and SEC guidance on conducting such assessments. Based on that evaluation, the Company's management concluded that during the period covered by this report its internal controls and procedures were effective.

## PART II OTHER INFORMATION

## Item Legal Proceedings.

1.

On May 1, 2003, the Company filed a lawsuit in the Supreme Court of British Columbia, Canada, against John Wells and Equity Trust, S.A. seeking the return of 100,000 shares of the Company's common stock and the repayment of a \$25,000 loan, which were provided to defendants for investment banking services consisting of securing a \$5 million loan and a \$25 million stock offering. Such services were not performed and in the proceeding the Company seeks return of such shares after defendant's failure to both return the shares voluntarily and repay the note. On May 7, 2003, the Company obtained an injunction freezing the transfer of the shares. On May 24, 2004, there was a hearing on defendant's motion to set aside the injunction, which motion was denied by the trial court on May 29, 2004. On the date of issuance, the share transaction was recorded as shares issued for services at fair market value, a value of \$0.80 per share. No amounts have been recorded as receivable in the Company's consolidated financial statements as the outcome of this claim is not determinable.

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

2.

None.

## Item Defaults Upon Senior Securities.

3.

None.

## Item Submission of Matters to a Vote of Security Holders.

4.

The annual meeting of the Company's shareholders was held on June 26, 2008. At the meeting the following persons were re-elected as directors for the upcoming year:

| Name               | Votes For | Votes Against | Votes Abstained |
|--------------------|-----------|---------------|-----------------|
| Daniel B. O'Brien  | 9,942,926 | 13,872        | 32,112          |
| Dr. Robert O'Brien | 9,777,193 | 177,262       | 34,365          |
| John H. Bientjes   | 9,939,123 | 15,332        | 34,365          |
| Dale Friend        | 9,939,123 | 15,332        | 34,365          |
| Eric Hodges        | 9,940,876 | 13,579        | 34,365          |

At the meeting, the following proposals were ratified by the shareholders:

1. Vote to approve the granting of the following options to officers and directors:

A) John H. Bientjes 5,000 options to buy common shares with a strike price of \$3.60/share, vesting on December 31, 2008 and expiring on December 18, 2013.

B)

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Dale 5,000 options to buy common shares with a strike price of \$3.60/share, vesting on December  
Friend 31, 2008 and expiring on December 18, 2013.

C) Eric Hodges 5,000 options to buy common shares with a strike price of \$3.60/share, vesting on December  
31, 2008 and expiring on December 18, 2013.

2. Approval of Annual Report

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3. Vote to ratify the selection of Cinnamon Jang Willoughby & Company as the Company's independent registered public accountants for the year ending December 31, 2008.

The following is a tabulation of the votes cast with respect to these proposals:

| Proposal | Votes For | Votes Against | Votes Abstained |
|----------|-----------|---------------|-----------------|
| 1A       | 7,798,628 | 34,448        | 5,260           |
| 1B       | 7,797,828 | 34,948        | 5,560           |
| 1C       | 7,797,328 | 35,748        | 5,260           |
| 2        | 9,975,357 | 10,696        | 2,770           |
| 3        | 9,939,156 | 21,896        | 27,769          |

Item Other Information.

5.

None.

Item Exhibits.

6.

| Number | Description   |
|--------|---|
| 3.1    | Amended and Restated Certificate of Incorporation of the registrant. (1)  |
| 3.2    | Bylaws of the registrant. (1)   |
| 31.1   | Certification of Principal Executive Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002.*                     |
| 31.2   | Certification of Principal Financial Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002.*                     |
| 32.1   | Certification of Principal Executive Officer Pursuant to 18 U.S.C. §1350 and §906 of the Sarbanes-Oxley Act of 2002.* |
| 32.2   | Certification of Principal Financial Officer Pursuant to 18 U.S.C. §1350 and §906 of the Sarbanes-Oxley Act of 2002.* |

\* Filed with this report.

(1) Incorporated by reference to the registrant's Registration Statement on Form 10-SB (SEC File. No. 000-29649) filed February 22, 2000.

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SIGNATURES

In accordance with the requirements of Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Flexible Solutions International, Inc.

October 9, 2008

By: /s/ Daniel B. O'Brien  
Name: Daniel B. O'Brien  
Title: President and Chief Executive Officer

By: /s/ Daniel B. O'Brien  
Name: Daniel B. O'Brien  
Title: President and Chief Executive Officer