REFLECT SCIENTIFIC INC
Form 10-Q
November 17, 2008

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

For the quarterly period ended September 30, 2008

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

For the transition period from __________ to __________

Commission File Number 000-31377

Reflect Scientific, Inc.

(Exact name of registrant as specified in its charter)

Utah

87-0642556

(State or other jurisdiction of

(IRS Employer Identification No.)

incorporation or organization)

<u>1270 South 1380 West Orem, Utah 84058</u>

(Address of principal executive offices) (Zip Code)

<u>(801) 226-4100</u>

(Registrant s telephone number, including area code)

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

Yes [X] No [ ]

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large Accelerated filer ¨

Accelerated filer ¨

Non-accelerated filer ¨ (Do not check if a smaller reporting company)

Smaller reporting company x

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

Yes [ ] No [X]

Indicate the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable date.

34,423,802 shares of $0.01 par value common stock on November 4, 2008

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

## Part I - FINANCIAL INFORMATION

### Item 1. Financial Statements

**Reflect Scientific, Inc.**

FINANCIAL STATEMENTS

(UNAUDITED)

September 30, 2008

The financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. However, in the opinion of management, all adjustments (which include only normal recurring accruals) necessary to present fairly the financial position and results of operations for the periods presented have been made. These financial statements should be read in conjunction with the accompanying notes, and with the historical financial information of the Company.

**REFLECT SCIENTIFIC, INC.**

**CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

**September 30, 2008**

**REFLECT SCIENTIFIC, INC.**

Condensed Consolidated Balance Sheets

ASSETS

| | September 30, 2008 (Unaudited) | December 31, 2007 (Audited) |
|---|---|---|
| CURRENT ASSETS | | |
| Cash | $ 600,834 | $ 1,154,162 |
| Accounts receivable | 1,199,623 | 1,371,770 |
| Other receivables | 36,170 | 28,517 |
| Inventory | 1,646,284 | 727,970 |
| Prepaid assets | 129,998 | 168,396 |
| Total Current Assets | 3,612,909 | 3,450,815 |
| FIXED ASSETS, NET | 274,722 | 259,884 |
| OTHER ASSETS | | |
| Intangible assets, net | 5,574,512 | 5,849,036 |
| Deferred tax asset | 38,000 | 38,000 |
| Unbilled receivables | 397,718 | - |
| Long term prepaid asset | 108,889 | 190,555 |
| Deposits | 29,944 | 29,945 |
| Total Other Assets | 6,149,063 | 6,107,536 |
| TOTAL ASSETS | $ 10,036,694 | $ 9,818,235 |

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

REFLECT SCIENTIFIC, INC.

Condensed Consolidated Balance Sheets (Continued)

LIABILITIES AND SHAREHOLDERS EQUITY

| | | September 30, 2008 (Unaudited) | | December 31, 2007 (Audited) |
|---|---|---|---|---|
| CURRENT LIABILITIES | | | | |
| Accounts payable | $ | 589,753 | $ | 432,392 |
| Short term loan | | 129,889 | | 147,530 |
| Royalty payable | | 73,550 | | 53,565 |
| Capital leases short-term portion | | 18,837 | | 20,016 |
| Interest payable | | 70,110 | | - |
| Debentures, net of Discount Warrant of $631,108 And Discount of Beneficial Conversion Feature of $331,517 | | 1,374,375 | | - |
| Accrued expenses | | 65,497 | | 179,778 |
| Contract billings in excess | | 53,270 | | 82,708 |
| Income taxes payable | | 400 | | 400 |
| Total Current Liabilities | | 2,375,681 | | 916,389 |
| LONG-TERM LIABILITIES | | | | |
| Debentures, net of Discount Warrant And Discount of Beneficial Conversion Feature | | - | | 618,750 |
| Capital leases long-term portion | | 23,670 | | 40,147 |
| Notes payable | | | | |
| Total Long-Term Liabilities | | 23,670 | | 658,897 |
| Total Liabilities | | 2,399,351 | | 1,575,286 |

SHAREHOLDERS EQUITY

| | | | |
|---|---|---|---|
| Preferred stock, $0.01 par value, authorized | | | |
| 5,000,000 shares; No shares issued and Outstanding | | - | - |
| Common stock, $0.01 par value, authorized | | | |
| 50,000,000 shares; 34,423,802 and 34,100,538 | | | |
| shares issued and outstanding respectively | | 344,238 | 341,006 |
| Additional paid in capital | | 16,757,688 | 16,512,094 |
| Accumulated deficit | | (9,464,583) | (8,610,151) |
| Total Shareholders Equity | | 7,637,343 | 8,242,949 |
| TOTAL LIABILITIES AND SHAREHOLDERS EQUITY | $ | 10,036,694 | 9,818,235 |

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

REFLECT SCIENTIFIC, INC.

Condensed Consolidated Statements of Operations

(Unaudited)

| | For the Three Months Ended September 30, | | For the Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2008 | 2007 | 2008 | 2007 |
| REVENUES | $ 2,548,942 | $ 1,383,614 | 7,790,028 | 5,939,251 |
| COST OF GOODS SOLD | 916,374 | 940,710 | 3,539,809 | 3,341,277 |
| GROSS PROFIT | 1,632,568 | 442,904 | 4,250,219 | 2,597,974 |
| OPERATING EXPENSES | | | | |
| Salaries and wages | 589,956 | 571,880 | 1,741,597 | 1,444,770 |
| Rent expense | 75,425 | 79,211 | 205,769 | 175,806 |
| General and administrative expense | 762,567 | 513,928 | 2,027,315 | 2,629,428 |
| Total Operating Expenses | 1,427,948 | 1,165,019 | 3,974,681 | 4,250,004 |
| OPERATING INCOME (LOSS) | 204,620 | (722,115) | 275,538 | (1,652,030) |
| OTHER INCOME (EXPENSE) | | | | |
| Interest income | 2,073 | 8,904 | 10,419 | 8,904 |
| Interest expense | (376,236) | (389,566) | (1,140,389) | (874,411) |
| Total Other Expenses | (374,163) | (380,662) | (1,129,970) | (865,507) |
| NET LOSS BEFORE INCOME TAXES | (169,543) | (1,102,777) | (854,432) | (2,517,537) |
| Income tax benefit (expense) | - | - | - | - |

| | | | | |
|---|---|---|---|---|
| NET LOSS | $ (169,543) | $ (1,102,777) | $ (854,432) | $ (2,517,537) |
| BASIC AND FULLY DILUTED LOSS PER SHARE | $ (0.00) | $ (0.03) | $ (0.02) | $ (0.08) |
| WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING | 34,423,739 | 34,963,927 | 34,313,027 | 31,780,093 |

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

REFLECT SCIENTIFIC, INC.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

For the Nine Months Ended

September 30,

| | | 2008 | | 2007 |
|---|---|---|---|---|
| Net loss | $ | (854,432) | $ | (2,517,537) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | | | |
| Depreciation | | 44,029 | | 36,108 |
| Amortization of Debenture Discount & Intangibles | | 1,168,149 | | 528,927 |
| Fair value of warrants issued | | 29,943 | | - |
| Common stock issued for services | | - | | 484,574 |
| Common stock issued for interest | | 3,722 | | - |
| Common stock issued for prepaid services | | - | | - |
| Changes in operating assets and liabilities: | | | | |
| (Increase) decrease in accounts receivable | | 172,146 | | (765,794) |
| Increase in inventory | | (918,314) | | (226,500) |
| Increase in unbilled receivables contract billings | | (397,718) | | (24,380) |
| Increase in other receivables | | (7,653) | | - |
| Increase in income tax receivable | | - | | - |
| (Increase) decrease in prepaid asset | | 120,065 | | 260,756 |
| Decrease in other assets | | - | | (29,944) |
| Decrease in billings in excess contract billings | | (29,436) | | - |
| Increase in accounts payable and accrued expenses | | 204,272 | | 370,044 |
| Net Cash Used by Operating Activities | | (465,227) | | (1,883,746) |
| CASH FLOWS FROM INVESTING ACTIVITIES | | | | - |
| Cash paid for fixed assets | | (58,867) | | (11,585) |
| Net Cash Used by Investing Activities | | (58,867) | | (11,585) |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | | |
| Payments on notes payable | | (11,593) | | 12,437 |
| Lines of Credit | | (17,641) | | - |

| | | | | |
|---|---|---|---|---|
| Proceeds from issuance of debenture | | - | | 2,500,000 |
| Proceeds from common stock issuance | | - | | 447,605 |
| Net Cash from Financing Activities | | (29,234) | | 2,960,042 |
| NET INCREASE (DECREASE) IN CASH | | (553,328) | | 1,064,712 |
| CASH AT BEGINNING OF PERIOD | | 1,154,162 | | 271,038 |
| CASH AT END OF PERIOD | $ | 600,834 | $ | 1,335,750 |

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

REFLECT SCIENTIFIC, INC.

Condensed Consolidated Statements of Cash Flows (continued)

(Unaudited)

| | | | | |
|---|---|---|---|---|
| SUPPLEMENTAL CASH FLOW INFORMATION: | | | | |
| Cash Paid For: | | | | |
| Interest | $ | 748,370 | $ | 8,859 |
| Income taxes | $ | - | $ | - |
| NON-CASH FINANCING ACTIVITIES: | | | | |
| Stock issued pursuant to Company mergers | $ | - | $ | 2,435,870 |
| Common stock subscription receivable issued | $ | - | $ | 484,574 |
| Common stock issued for services | $ | - | $ | 490,000 |
| Shareholder debt forgiveness | $ | 3,500 | $ | - |
| Common stock issued for accrued interest | $ | 73,661 | $ | - |

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

**REFLECT SCIENTIFIC, INC.**

Notes to the Condensed Consolidated Financial Statements

September 30, 2008

NOTE 1 - BASIS OF FINANCIAL STATEMENT PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company pursuant to accounting principles generally accepted in the United States of America. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted in accordance with rules and regulations of the Securities and Exchange Commission. The information furnished in the interim condensed consolidated financial statements include normal recurring adjustments and reflects all adjustments, which, in the opinion of management, are necessary for a fair presentation of such financial statements. Although management believes the disclosures and information presented are adequate to make the information not misleading, it is suggested that these interim condensed consolidated financial statements be read in conjunction with the Company s most recent audited consolidated financial statements and notes thereto included in its December 31, 2007 financial statements. Operating results for the three and nine months ended September 30, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008.

NOTE 2 - ORGANIZATION AND DESCRIPTION OF BUSINESS

Cole, Inc. (the Company) was incorporated under the laws of the State of Utah on November 3, 1999. The Company was organized to engage in any lawful activity for which corporations may be organized under the Utah Revised Business Corporation Act. On December 30, 2003 the Company changed its name to Reflect Scientific, Inc.

Reflect Scientific, Inc. a California corporation, was incorporated on September 14, 1993, under the laws of California to engage in the manufacture of test kits for use in scientific studies.

On December 30, 2003, pursuant to an Agreement and Plan of Reorganization, the Company completed a reverse merger with the shareholders of Reflect Scientific, Inc. in which it acquired 100% of Reflect Scientific, Inc., a California corporation in exchange for 22,914,949 common shares of the Company. The terms of the acquisition are detailed in an 8-K filing dated December 31, 2003. Under the terms of the agreement, the President of Reflect Scientific, Inc. became the President of the Company and was elected to the Board of Directors. The acquisition was accounted for as a recapitalization of Reflect Scientific, Inc. because the members of Reflect Scientific, Inc. controlled the Company after the acquisition. Reflect Scientific, Inc. was treated as the acquiring entity for accounting purposes and Cole, Inc. was the surviving entity for legal purposes. There was no adjustment to the carrying values of the assets or liabilities of Reflect Scientific, Inc. and no goodwill was recorded. The operations for the year ended December 31, 2007 and 2006 are those of Reflect Scientific, Inc. Effective January 19, 2007 the Company finalized an Agreement and Plan of Merger agreement with All Temp Engineering, Inc. Effective March 6, 2007, the Company finalized an Agreement and Plan of Merger agreement with Image Labs, International. The terms of the agreements are detailed in a 10-QSB filing dated September 30, 2007. The Company entered into these mergers after considering All Temp s and Image Lab s business history, financial condition, and intellectual property. The Company has a desire to expand its services, attract and retain talented technical personnel, and the Company believed there were strategic and financial advantages to combining the businesses.

**REFLECT SCIENTIFIC, INC.**

Notes to the Condensed Consolidated Financial Statements

September 30, 2008

NOTE 3 CONVERTIBLE DEBENTURES AND WARRANTS

On June 29, 2007, the Company entered into an agreement to sell $2,500,000 in 12% senior convertible debentures with a maturity date of June 29, 2009, with interest due quarterly. At the closing, the Company prepaid the first quarterly interest payment out of the proceeds of the offering from escrow and placed in escrow the second quarterly interest payment for a total of $150,000. The agreement allows for the Company to pay the interest in cash or in duly authorized, validly issued, fully paid and non-assessable shares of common stock at the interest conversion rate, or a combination thereof.

The debentures have a conversion price of $0.65. If the Company, at any time while the debenture is outstanding, pays stock dividends, subdivides outstanding shares, sells or grants any option to purchase or dispose of common stock at an effective price lower than the conversion price, issue rights, options or warrants at a price lower than the conversion price, etc., the Company shall promptly deliver to each Holder a notice setting forth the conversion price after such adjustment and provide a brief statement of facts requiring such adjustment. In addition, if the volume weighted average price for each of any 20 consecutive trading days exceeds 250% of the conversion price, the Company may, within one trading day deliver a written notice to the holder and force the holder to convert a principal amount of the debenture equal to all or part of the holder s portion of the forced conversion amount.

The agreement also provides for the issuance of 1,923,077 A warrants and 1,923,077 B warrants. The warrants are exercisable at a price of $0.80 per share for the A warrant and $1.00 per share for the B warrant and expire September 29, 2012. The Company valued the warrants using the Black-Scholes option pricing model. For the purpose of the valuation of the warrants, the Company calculated a volatility of 66.48% on its common stock and used the U. S. Treasury bill rate of 4.94% for its risk free rate. Then the Company allocated a portion of the proceeds to the warrants, based on the relative fair value basis, in the amount of $1,639,029 which is recognized as a contra liability account and will be amortized as interest expense over the 2 year term of the agreement. The intrinsic value of beneficial conversion of the debentures was valued at $5,677,491, which exceeds the effective value of the debentures of $860,971. Therefore, the discount assigned to the beneficial conversion feature is limited to $860,971 and is recognized as a contra liability account and will be amortized as interest expense over the 2 year term of the agreement.

As payment for services provided, the Company also issued 192,308 A warrants and 192,308 B warrants which were valued at $475,925 using the Black-Scholes option pricing model and expensed in the current period.

**REFLECT SCIENTIFIC, INC.**

Notes to the Condensed Consolidated Financial Statements

September 30, 2008

NOTE 3 CONVERTIBLE DEBENTURES AND WARRANTS (continued)

The debentures and warrants have anti-dilution protections, and the Company has agreed to certain registration rights for the resale of the shares of common stock underlying the debentures and warrants.

A summary of the status of the Company s outstanding stock warrants as of September 30, 2008 and changes during the period then ended is presented below:

| | | 2008 | |
|---|---|---|---|
| | | Weighted Average Exercise Price | |
| | Shares | | |
| Outstanding, beginning of year | 4,230,770 | $ | .90 |
| Granted | - | | - |
| Expired/Cancelled | - | | - |
| Exercised | - | | - |
| Outstanding September 30, 2008 | 4,230,770 | $ | .90 |
| Exercisable | 4,230,770 | $ | .90 |

| | **Outstanding** | **Exercisable** |
|---|---|---|

| Range of Exercise Prices | | Number outstanding at September 30, 2008 | Weighted Average Remaining Contractual Life | Number Exercisable at September 30, 2008 |
|---|---|---|---|---|
| **$** | **0.80** | **2,115,385** | **4.00** | **2,115,385** |
| | **1.00** | **2,115,385** | **4.00** | **2,115,385** |
| | | **4,230,770** | | **4,230,770** |

NOTE 4 EQUITY TRANSACTIONS

During the nine month period ended September 30, 2008, the Company issued 212,307 shares of its common stock for the conversion of $138,000 debt pursuant to the convertible debenture agreement dated September 29, 2007.

During the nine month period ended September 30, 2008, the Company issued 110,957 shares of its common stock for interest payable.

NOTE 5    COMMON STOCK OPTIONS

On December 31, 2007, the Company s board of directors approved an equity plan. The equity plan known as the 2007 Equity Incentive Plan (the Plan ) reserves up to 6,000,000 shares of the Company s authorized common stock for issuance to officers, directors, employees and consultants under the terms of the Plan. The Plan permits the board of directors to issue stock options and restricted stock.

In conjunction with its employee stock option plan, the company issued 66,660 options to employees. These options had a fair value of $29,930 and were expensed when issued. The options were issued in September 2008.

The fair value of each option granted under the Plan is estimated on the date of grant, using the Black-Scholes option pricing model, based on the following weighted average assumptions:

| | September 30, 2008 | |
|---|---|---|
| Expected life (years) | 5.0 | |
| Expected stock price volatility | 65.74 - 66.27 | % |
| Expected dividend yield | 0.0 | % |
| Risk-free interest rate | 3.38 3.41 | % |

The risk-free interest rate is based upon the U.S. Treasury yield curve at the time of grant for the respective expected life of the option. The expected life (estimated period of time outstanding) of options was estimated. The expected volatility of the Company s options was calculated using historical data. Expected dividend yield was not considered in the option pricing formula since the Company does not pay dividends and has no current plans to do so in the future. If actual periods of time outstanding and rate of forfeitures differs from the expected rates, the Company may be required to make additional adjustments to compensation expense in future periods.

A summary of the status of the Company s outstanding stock options as of September 30, 2008 and changes during the period then ended is presented below:

| 2008 | | |
|---|---|---|
| | | Weighted Average Exercise Price |

| | Shares | | |
|---|---|---|---|
| Outstanding, beginning of year | 5,000,000 | $ | 1.32 |
| Granted | 66,660 | | .94 |
| Expired/Cancelled | - | | - |
| Exercised | - | | - |
| Outstanding at September 30, 2008 | 5,066,660 | $ | 1.31 |
| Exercisable | 5,066,660 | $ | 1.31 |

| | Outstanding | | Exercisable |
|---|---|---|---|
| Range of Exercise Prices | Number outstanding at September 30, 2008 | Weighted Average Remaining Contractual Life | Number Exercisable at September 30, 2008 |
| $ 1.32 | 4,800,000 | 4.50 | 4,800,000 |
| 1.20 | 200,000 | 4.50 | 200,000 |
| 0.85 | 52,660 | 5.00 | 52,660 |
| 1.30 | 14,000 | 5.00 | 14,000 |
| | 5,066,660 | | 5,066,660 |

The total fair value of options vested was $3,383,487 as of September 30, 2008. As of September 30, 2008, there was no unrecognized compensation cost related to non-vested stock options granted under the Plan

NOTE 6 RECENT ACCOUNTING PRONOUNCEMENTS

In December 2007, the FASB issued SFAS No. 141(R), Business Combinations. SFAS No. 141(R) changes the accounting for and reporting of business combination transactions in the following way: Recognition with certain exceptions, of 100% of the fair values of assets acquired, liabilities assumed, and non controlling interests of acquired businesses; measurement of all acquirer shares issued in consideration for a business combination at fair value on the acquisition date; recognition of contingent consideration arrangements at their acquisition date fair values, with subsequent changes in fair value generally reflected in earnings; recognition of pre-acquisition gain and loss contingencies at their acquisition date fair value; capitalization of in-process research and development (IPR&D) assets acquired at acquisition date fair value; recognition of acquisition-related transaction costs as expense when incurred; recognition of acquisition-related restructuring cost accruals in acquisition accounting only if the criteria in Statement No. 146 are met as of the acquisition date; and recognition of changes in the acquirer s income tax valuation allowance resulting from the business combination separately from the business combination as adjustments to income tax expense. SFAS No. 141(R) is effective for the first annual reporting period beginning on or after December 15, 2008 with earlier adoption prohibited. The adoption of SFAS No. 141(R) will affect valuation of business acquisitions made in 2009 and forward.

In December 2007, the FASB issued SFAS No. 160 "Noncontrolling Interest in Consolidated Financial Statements an Amendment of ARB 51" (SFAS 160). SFAS 160 clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements.  It also requires consolidated net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest, and 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.  SAFS 160 is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008.  Earlier adoption is prohibited.  We do not anticipate a material impact upon adoption.



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In March 2008, the FSAB issued FASS No. 161, Disclosures about Derivative Instruments and Hedging Activities. SFAS 161 is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity's financial position, financial performance, and cash flows. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. We do not anticipate a material impact upon adoption.

In May 2008,the FASB issued SFAS No. 162, "The Hierarchy of Generally Accepted Accounting Principles." This statement identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles ("GAAP") in the United States (the "GAAP hierarchy"). This statement is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, "The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles". The Company does not expect this statement to have any effect on our financial position or results of operations.

In May 2008, FASB issued SFAS 163, Accounting for Financial Guarantee Insurance Contracts - an interpretation of FASB Statement No. 60. SFAS 163 clarifies how Statement 60 applies to financial guarantee insurance contracts, including the recognition and measurement of premium revenue and claim liabilities. This Statement also requires expanded disclosures about financial guarantee insurance contracts. SFAS 163 is effective for fiscal years beginning on or after December 15, 2008, and interim periods within those fiscal years. The Company does not expect that the adoption of SFAS 163 will have a material impact on its consolidated financial statements.

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

Special Note Regarding Forward-Looking Statements

This periodic report contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to the Plan of Operations provided below, including information regarding the Company s financial condition, results of operations, business strategies, operating efficiencies or synergies, competitive positions, growth opportunities, and the plans and objectives of management. The statements made as part of the Plan of Operations that are not historical facts are hereby identified as "forward-looking statements."

Critical Accounting Policies and Estimates

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the unaudited Financial Statements and accompanying notes. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from these estimates under different assumptions or conditions. The Company believes there have been no significant changes during the nine month periods ended September 30, 2008 and 2007, to the items disclosed as significant accounting policies in management's Notes to the Financial Statements in the Company's Annual Report on Form 10-KSB for the year ended December 31, 2007.

Plan of Operation and Business Growth

Over the next twelve months our focus will be on the commercialization of products acquired and developed over the last several years. Included in this focus will be the continued development and commercialization of our ultra low temperature refrigerator line. Additionally, we will continue to develop and expand our focus on solutions and services to retrofit server and computer rooms to help reduce the cost of cooling such rooms as well as provide a more reliable way to cool such rooms. We also will continue to focus on the expansion of our detector line and contract manufacturing operations.

Management focus over the last several years was on the acquisition and development of our product lines. Management now feels they have the core product lines in place to now refocus its efforts on the commercialization of the product lines. As such much of the focus over the next twelve months will be on marketing our products and expanding our customer base.

Results of Operations

September 30, 2008 and 2007

Our revenues increased from the quarter ended September 30, 2007, of $1,383,614 to $2,548,942 for the quarter ended September 30, 2008.  as our products gain more commercial acceptance.

Our cost of goods sold decreased in the quarter ending September 30, 2008, as compared to September 30, 2007 to $916,374 from $940,710 .   Overall, as a percentage of sales, our cost of goods sold was approximately 36% for the three months ended September 30, 2008 compared to 68% for the quarter ended September 30, 2007.  This gives us gross profit percentages of 64% and 32%, respectively.  We anticipate the cost of goods sold percentage and gross profit percentage to vary by quarter depending on which products make up the largest percentage of sales during the quarter.  We anticipate these percentages to become more stable as our sales for all products continue to increase.

Although sales increased for the nine month period, the increase was not sufficient to offset additional expenses as we again expanded our operations during the quarter ended September 30, 2008. Salaries and wages increased to $589,956 during the quarter ended September 30, 2008, compared to $571,880 for the quarter ended September 30, 2007. This increase reflects the closing of all of our acquisitions and the hiring of additional personnel. We felt it was necessary to retain additional personnel in an effort to effectively market our products and take advantage of business opportunities. Rent expense also increased as we began covering the expenses of businesses acquired in the first quarter of 2007.

With the increase in operating expenses from $1,165,019 for the quarter ended September 30, 2007 to $1,427,948 for the quarter ended September 30, 2008, our net loss decreased to $169,543 from $1,102,777 for the comparable period in 2007. We expect that as sales continue to increase, we will be able to continue to reduce our net loss this year.

Interest expense was $376,236 for the quarter ended September 30, 2008. This interest expense primarily related to interest on our debentures of $73,833 for the quarter and $302,403 related to the amortization of the discounts on the debenture.

Seasonality and Cyclicality

We do not believe our business is cyclical.

Liquidity and Capital Resources

Our cash resources at September 30, 2008, were $600,834, with accounts receivable of $1,199,623 and inventory of $1,646,284. We have relied on revenues and sales of equity and debt securities for cash resources. Our working capital on September 30, 2008, was $1,237,228 compared to $2,534,426 on December 31, 2007. This decrease is due to our convertible debenture now becoming due in less than twelve months and being classified as a current asset. In June 2009, the debenture will be due and the total amount owed will be $2,337,000, less any future conversions. If the debentures are not converted, we would probably have to seek some additional debt or equity financing to help repay the debenture. The amount of debt or equity financing required will be dependent on how our operations perform over the next nine months. If sales continue to increase, we may be able to repay part of the debentures with operating profits.We anticipate devoting some of the available cash to marketing programs that will increase sales over the next twelve months.

Historically, we have financed our working capital requirements through capital funding which have generated sufficient funds to offset shortfalls and cover losses. As we continue to expand our operations, we anticipate seeking additional capital through the sale of equity securities. It is highly likely, we will again seek additional capital in the equity markets. At this time we do not know the extent of the overall financing will need in the future. Financing will depend on how well our products are received in the marketplace.

Our long term liabilities were $ 23,670 on September 30, 2008 down from $658,897 on December 31, 2007.  This decrease is due to the change to the current liability classification for the debenture..

For the quarter ended September 30, 2008, our net cash used by operating activities was $465,227 which was down from $1,883,746 for the quarter ended September 30, 2007.  We were pleased with this reduction as it reflects our business operations are starting to cover our cash needs.

We anticipate losses to continue as we expand our sales efforts.  Since the products are new to the marketplace, we cannot predict with certainty how sales will be in upcoming quarters but we expect they will continue to increase and should start covering our expenses.

**Off-Balance Sheet Arrangements**

We have no off balance sheet arrangements as of September 30, 2008.

**Forward-looking Statements**

The Private Securities Litigation Reform Act of 1995 (the Act ) provides a safe harbor for forward-looking statements made by or on behalf of our Company. Our Company and our representatives may from time to time make written or oral statements that are forward-looking, including statements contained in this Annual Report and other filings with the Securities and Exchange Commission and in reports to our Company s stockholders. Management believes that all statements that express expectations and projections with respect to future matters, as well as from developments beyond our Company s control including changes in global economic conditions are forward-looking statements within the meaning of the Act. These statements are made on the basis of management s views and assumptions, as of the time the statements are made, regarding future events and business performance. There can be no assurance, however, that management s expectations will necessarily come to pass. Factors that may affect forward- looking statements include a wide range of factors that could materially affect future developments and performance, including the following:

Changes in Company-wide strategies, which may result in changes in the types or mix of businesses in which our Company is involved or chooses to invest; changes in U.S., global or regional economic conditions, changes in U.S. and global financial and equity markets, including significant interest rate fluctuations, which may impede our Company s access to, or increase the cost of, external financing for our operations and investments; increased competitive pressures, both domestically and internationally, legal and regulatory developments, such as regulatory actions affecting environmental activities, the imposition by foreign countries of trade restrictions and changes in international tax laws or currency controls; adverse weather conditions or natural disasters, such as hurricanes and earthquakes, labor disputes, which may lead to increased costs or disruption of operations.

This list of factors that may affect future performance and the accuracy of forward-looking statements are illustrative, but by no means exhaustive. Accordingly, all forward-looking statements should be evaluated with the understanding of their inherent uncertainty.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

This item is not required for Small Reporting Companies.

**Item 4T. Controls and Procedures.**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our President and CFO, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, our President and CFO concluded that our disclosure controls and procedures as of the end of the period covered by this report were effective such that the information required to be disclosed by us in reports filed under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms and (ii) accumulated and communicated to our management, including our President and CFO, as appropriate to allow timely decisions regarding disclosure. A controls system cannot provide absolute assurance, however, that the objectives of the controls system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

**Management s Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act). Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes of accounting principles generally accepted in the United States.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance of achieving their control objectives.

Our management, with the participation of the President and CFO, evaluated the effectiveness of our internal control over financial reporting as of September 30, 2008. Based on this evaluation, our management, with the participation of the President and CFO, concluded that, as of September 30, 2008, our internal control over financial reporting was effective.

**Changes in internal control over financial reporting**

There have been no changes in internal control over financial reporting.

## PART II - OTHER INFORMATION

### ITEM 1. Legal Proceedings

None

### ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds

**Recent Sales of Unregistered Securities**

We have not sold any restricted securities during the nine months ended September 30, 2008.

**Use of Proceeds of Registered Securities**

None; not applicable.

**Purchases of Equity Securities by Us and Affiliated Purchasers**

During the nine months ended September 30, 2008, we have not purchased any equity securities nor have any officers or directors of the Company.

### ITEM 3. Defaults Upon Senior Securities

We are not aware of any defaults upon senior securities.

**ITEM 4. Submission of Matters to a Vote of Security Holders**

No matters were submitted to a vote of security holders during the quarter ended September 30, 2008.

**ITEM 5. Other Information.**

None

**ITEM 6. Exhibits**

(a) Exhibits.

| Exhibit No. | Title of Document | Location if other than attached hereto |
|---|---|---|
| 3.1 | Articles of Incorporation | 10-SB Registration Statement* |
| 3.2 | Articles of Amendment to Articles of Incorporation | 10-SB Registration Statement* |
| 3.3 | By-Laws | 10-SB Registration Statement* |
| 3.4 | Articles of Amendment to Articles of Incorporation | 8-K Current Report dated December 31, 2003* |
| 3.5 | Articles of Amendment to Articles of Incorporation | 8-K Current Report dated December 31, 2003* |
| 3.6 | Articles of Amendment | September 30, 2004 10-QSB Quarterly Report* |
| 3.7 | By-Laws Amendment | September 30, 2004 10-QSB Quarterly Report* |
| 4.1 | Debenture | 8-K Current Report dated September 29, 2007* |
| 4.2 | Form of Purchasers Warrant | 8-K Current Report dated September 29, 2007* |
| 4.3 | Registration Rights Agreement | 8-K Current Report dated September 29, 2007* |
| 4.4 | Form of Placement Agreement | 8-K Current Report dated September 29, 2007* |
| 10.1 | Securities Purchase Agreement | 8-K Current Report dated September 29, 2007* |
| 10.2 | Placement Agent Agreement | 8-K Current Report dated September 29, 2007* |
| 14 | Code of Ethics | December 31, 2003 10-KSB Annual Report* |
| 21 | Subsidiaries of the Company | December 31, 2004 10-KSB Annual Report* |
| 31.1 | 302 Certification of Kim Boyce | |
| 31.2 | 302 Certification of David Strate | |
| 32 | 906 Certification | |

**Exhibits**

**Additional Exhibits Incorporated by Reference**

| | | |
|---|---|---|
| * | Reflect California Reorganization | 8-K Current Report dated December 31, 2003 |

| | | |
|---|---|---|
| * | JMST Acquisition | 8-K Current Report dated April 4, 2006 |
| * | Cryomastor Reorganization | 8-K Current Report dated September 27, 2006 |
| * | Image Labs Merger Agreement Signing | 8-K Current Report dated November 15, 2006 |
| * | All Temp Merger Agreement Signing | 8-K Current Report dated November 17, 2006 |
| * | All Temp Merger Agreement Closing | 8-KA Current Report dated November 17, 2006 |
| * | Image Labs Merger Agreement Closing | 8-KA Current Report dated November 15, 2006 |

* Previously filed and incorporated by reference.

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.

Reflect Scientific, Inc.

(Registrant)

Date:

November 17, 2008

By: /s/ Kim Boyce

Kim Boyce, CEO, President and Director

Date:

November 17, 2008

By: /s/ Tom Tait

Tom Tait, Vice President and Director

Date:

November 17, 2008

By: /s/ David Strate

David Strate, CFO