

First Aviation Services Inc.
Consolidated Financial Statements
For the Years Ended January 31, 2009 and 2008



DIXON HUGHES PLLC

Certified Public Accountants and Advisors

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First Aviation Services Inc.

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For the Years Ended January 31, 2009 and 2008

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Independent Auditors' Report

The Board of Directors and Stockholders
First Aviation Services Inc.

We have audited the accompanying consolidated balance sheets of First Aviation Services Inc. and Subsidiaries (the "Company") as of January 31, 2009 and 2008, and the related consolidated statements of operations, stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We did not audit the 2009 and 2008 financial statements of API Asia Pacific, Inc. and API China, Inc. (wholly-owned subsidiaries) with assets of \$3,484,155 and \$4,943,632 at January 31, 2009 and 2008, respectively, and revenues of \$10,277,887 and \$10,453,871, respectively for the years then ended and net losses of \$166,712 and \$898,539, respectively, for the years then ended. The 2009 and 2008 financial statements of API Asia Pacific, Inc. and API China, Inc. were audited by other auditors whose reports were furnished to us, and our opinion, insofar as it relates to the amounts included for API Asia Pacific, Inc. and API China, Inc. is based solely on the reports of other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances but not for expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the 2009 and 2008 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of First Aviation Services Inc. and Subsidiaries as of January 31, 2009 and 2008, and the consolidated results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

September 4, 2009, except for Note 5, as to
which the date is October 23, 2009

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First Aviation Services Inc.

Consolidated Balance Sheets (in thousands, except share and per share amounts)

January 31, 2009 and 2008

	2009	2008 (as restated)
Assets		
Current assets:		
Cash and cash equivalents	\$ 1,304	\$ 750
Trade receivables, net	14,492	17,096
Inventories, net	29,471	29,455
Prepaid expenses and other	1,362	1,415
Total current assets	46,629	48,716
Plant and equipment, net	3,253	4,064
Total assets	\$ 49,882	\$ 52,780
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 11,651	\$ 10,654
Accrued compensation and related expenses	290	762
Other accrued liabilities	1,280	1,480
Revolving line of credit	20,630	20,374
Note payable	537	598
Total current liabilities	34,388	33,868
Subordinated debt:		
Related party - JEM III LLC	2,000	2,000
Note payable, less current portion	-	445
Total liabilities	36,388	36,313
Stockholders' equity		
Common stock, \$0.01 par value, 25,000,000 shares authorized (reduced to 10,000,000 shares authorized in April 2008), 9,135,699 shares issued	91	91
Additional paid-in capital	38,288	38,782
Deficit	(16,761)	(14,227)
Accumulated other comprehensive income	229	835
	21,847	25,481
Less: treasury stock, at cost, 1,601,130 and 1,713,774 shares, respectively	(8,353)	(9,014)
Total stockholders' equity	13,494	16,467
Total liabilities and stockholders' equity	\$ 49,882	\$ 52,780

See notes to consolidated financial statements.

First Aviation Services Inc.

Consolidated Statements of Operations (in thousands, except share and per share amounts)

For the Years Ended January 31, 2009 and 2008

	2009	2008
Net sales	\$ 114,244	\$ 125,223
Cost of sales	(95,037)	(106,012)
Gross profit	19,207	19,211
Selling, general and administrative expenses	18,723	19,725
Corporate expenses	1,647	1,841
Loss from operations	(1,163)	(2,355)
Interest income	4	7
Interest expense and other, net	(1,374)	(1,399)
Loss before income taxes	(2,533)	(3,747)
Benefit for income taxes	(1)	-
Net loss	\$ (2,534)	\$ (3,747)
<i>Basic net loss per share, and net loss per share - assuming dilution:</i>		
Basic net loss per share	\$ (0.34)	\$ (0.51)
Net loss per share - assuming dilution	\$ (0.34)	\$ (0.51)
Weighted average shares outstanding - basic	7,465,583	7,409,332
Weighted average shares outstanding - assuming dilution	7,465,583	7,409,332

See notes to consolidated financial statements.

First Aviation Services, Inc.

Consolidated Statements of Stockholders' Equity

(in thousands, except share amounts)

For the Years Ended January 31, 2009 and 2008

	Comprehensive Income (Loss)	Common Stock		Additional Paid-in Capital	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income (Loss)	Sub-Total	Treasury Stock		Total
		Number of Shares	Amount					Number of Shares	Amount	
Balances at February 1, 2007, as restated		7,378,851	\$ 91	\$ 38,787	\$ (10,480)	\$ 460	\$ 28,858	1,756,848	\$ (9,137)	\$ 19,721
Shares issued to directors		43,074	-	(48)	-	-	(48)	(43,074)	123	75
Other equity based compensation		-	-	43	-	-	43	-	-	43
Other comprehensive income	\$ 375	-	-	-	-	375	375	-	-	375
Net loss	(3,747)	-	-	-	(3,747)	-	(3,747)	-	-	(3,747)
	<u>\$ (3,372)</u>									
Balances at January 31, 2008, as restated		7,421,925	91	38,782	(14,227)	835	25,481	1,713,774	(9,014)	16,467
Shares issued to directors		77,634	-	(575)	-	-	(575)	(77,634)	661	86
Other equity based compensation		35,010	-	81	-	-	81	(35,010)	-	81
Other comprehensive loss	\$ (606)	-	-	-	-	(606)	(606)	-	-	(606)
Net loss	(2,534)	-	-	-	(2,534)	-	(2,534)	-	-	(2,534)
	<u>\$ (3,140)</u>									
Balances at January 31, 2009		<u>7,534,569</u>	<u>\$ 91</u>	<u>\$ 38,288</u>	<u>\$ (16,761)</u>	<u>\$ 229</u>	<u>\$ 21,847</u>	<u>1,601,130</u>	<u>\$ (8,353)</u>	<u>\$ 13,494</u>

First Aviation Services Inc.

Consolidated Statements of Cash Flows (in thousands)

For the Years Ended January 31, 2009 and 2008

	2009	2008
Cash flows from operating activities		
Net loss	\$ (2,534)	\$ (3,747)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	1,521	1,678
Equity based compensation	167	118
Provision for bad debts	(142)	(1,023)
Provision for excess and obsolete inventory	(1,011)	(965)
(Gain) loss on sale of plant and equipment	(5)	2
Other	-	-
Change in working capital assets/liabilities:		
Trade receivables	2,746	4,774
Inventories	795	2,730
Prepaid expenses and other assets	53	71
Accounts payable	997	(2,646)
Other accrued liabilities	(672)	(1,734)
Net cash provided by (used in) operating activities	1,915	(742)
Cash flows from investing activities		
Purchases of plant and equipment and other assets	(702)	(655)
Proceeds from disposals of plant and equipment and other assets	-	-
Net cash used in investing activities	(702)	(655)
Cash flows from financing activities		
Borrowings (repayments) on revolving line of credit, net	256	(1,726)
Issuance of subordinated debt	-	3,000
Repayment on subordinated debt	-	(1,000)
Repayments on note payable	(506)	(253)
Net cash provided by (used in) financing activities	(250)	21
Effect of exchange rate changes on cash and cash equivalents	(409)	381
Net change in cash and cash equivalents	554	(995)
Cash and cash equivalents at the beginning of the year	750	1,745
Cash and cash equivalents at the end of the year	\$ 1,304	\$ 750
Supplemental cash flow disclosures		
Cash paid for:		
Interest	\$ 1,238	\$ 1,827
Income taxes paid, net	\$ -	\$ -

See notes to consolidated financial statements.

First Aviation Services Inc.

Notes to Consolidated Financial Statements (dollar amounts in thousands, except share and per share amounts)

1. Business

First Aviation Services Inc. ("First Aviation"), through its wholly-owned subsidiaries, Aerospace Products International, Inc. ("API"), Aerospace Products International, Ltd. (Canada) ("API Ltd."), API Asia Pacific, Inc. ("API Asia Pacific"), API Europe, Ltd. ("API Europe"), and API China, Inc. ("API China"), (collectively the "Company"), is one of the leading suppliers of products and services to the aerospace industry worldwide; including the provisioning of aircraft parts and components, and supply chain management services. The Company also performs overhaul and repair services for wheels, brakes and starter/generators, and builds custom hose assemblies. The Company has its headquarters in Westport, Connecticut.

First Aviation was formed in March 1995 to acquire the capital stock of National Airmotive Corporation ("NAC"). On March 5, 1997, the Company completed an initial public offering of its common stock. A portion of the proceeds was used to acquire API's business from AMR Combs, Inc.

2. Restatement

During fiscal 2009, management became aware of certain misstatements for the year ended January 31, 2007, related to its conversion to new enterprise software and accounting for intercompany in-transit inventory. Management has corrected these errors by restating the 2008 consolidated financial statements, as follows:

	<u>Previously Reported</u>	<u>Restated</u>
Inventories	\$ 30,751	\$ 29,455
Deficit:		
Beginning of year	(9,184)	(10,480)
End of year	(12,931)	(14,227)

3. Summary of Significant Accounting Policies

Consolidation

The accompanying consolidated financial statements include the accounts of First Aviation and its subsidiaries. Significant intercompany balances and transactions have been eliminated in consolidation.

3. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates, and the differences may be significant.

Revenue Recognition

The Company's net sales consist of sales and services to the aviation industry, including parts and components supply services, supply chain management services, and component overhaul and repair services. Net sales are recorded when parts and components are shipped and title transfers to the customer, when overhaul and repair services are completed and the item is shipped back to the customer, or when supply chain management services have been provided to the customer. The terms and nature of supply chain management services provided are stipulated in a long-term contract between the Company and the customer. The Company provides its facilities, personnel and systems to provide cost effective services to the customer. In providing services where the Company distributes inventory on behalf of its customer, the Company may use its own inventory or hold its customers' inventory without taking ownership of such inventory. The Company, when providing services to handle customers' inventory without taking ownership, takes a fee based on the cost of providing services, and not on the sales value of the product.

Accounts Receivable

The Company provides credit in the form of trade accounts receivable to its customers. The Company generally does not require collateral to support domestic customer receivables. Receivables arising from export activities may be supported by foreign credit insurance. The Company performs ongoing credit evaluations of its customers and maintains allowances that management believes are adequate for potential credit losses. The allowance for doubtful accounts was \$1,013 and \$992 at January 31, 2009 and 2008, respectively.

Cash and Cash Equivalents

Cash and cash equivalents at any time may consist of a combination of demand deposits, money market or short-term, high-grade bond funds and short-term certificates of deposit purchased with original maturities of less than three months.

3. Summary of Significant Accounting Policies (continued)

Inventories

Inventories generally consist of aircraft parts and components and are stated at the lower of cost using the average cost method, or market. Provisions are made for the estimated effect of obsolete and slow moving inventories using a methodology based upon financial formulas that takes into account quantities, costs, the age of the inventory on hand, historical and projected sales, and other inventory movements, adjusted for known or estimated factors such as new product lines and product return allowances. The allowance for obsolete and slow moving inventories was \$4,425 and \$5,437 at January 31, 2009 and 2008, respectively.

Plant and Equipment

Plant and equipment are stated at cost, less an allowance for depreciation. Additions and improvements that materially increase the productive capacity or extend the useful life of an asset are added to the cost of the asset. Expenditures for normal maintenance and repairs are charged to expense as incurred.

Depreciation of plant and equipment is computed using the straight-line method over the estimated useful lives of the assets, which range from 3 to 15 years. Leasehold improvements are amortized over the shorter of the estimated life of the improvement or the term of the related lease.

Long-Lived Assets

Long-lived assets are reviewed for impairment when circumstances indicate the carrying value of an asset may not be recoverable. An impairment is recognized when the estimated undiscounted cash flows associated with the asset or group of assets is less than the carrying value. If impairment exists, an impairment loss is recognized as the difference between the carrying value of the asset and its fair value. Fair value is determined based on quoted market values, discounted cash flows or internal and external appraisals, as applicable. No asset impairments were recorded during the years ended January 31, 2009 and 2008.

Income Taxes

The Company uses the liability method to account for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities, and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse. The Company records valuation allowances against deferred tax assets as it is more likely than not that the deferred tax assets will not be realized.

The Company adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of Statement No. 109*, on February 1, 2007, which had no material impact on the consolidated financial statements.

3. Summary of Significant Accounting Policies (continued)

Income Taxes (continued)

The Company recognizes liabilities for uncertain income tax positions based on a two-step process. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step requires management to estimate and measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. It is inherently difficult and subjective to estimate such amounts, as management must determine the probability of various possible outcomes. Management reevaluates these uncertain tax positions on a quarterly basis or when new information becomes available. These reevaluations are based on factors including, but not limited to, changes in facts or circumstances, changes in tax law, successfully settled issues under audit, and new audit activity. Such a change in recognition or measurement could result in the recognition of a tax benefit or an increase to the tax accrual.

Interest related to income tax liabilities is included in interest expense, and if applicable, penalties are recognized as a component of income tax expense.

The Company does not have any uncertain tax positions at January 31, 2009 and 2008.

Accumulated Other Comprehensive Income (Loss)

The accumulated other comprehensive loss arose from the translation of accounts into U. S. dollars where the functional currency is the Canadian dollar (API Ltd.). Comprehensive loss during the years ended January 31, 2009 and 2008, was impacted due to changes in the value of the Canadian dollar relative to the U.S. dollar, as follows:

	<u>2009</u>	<u>2008</u>
Net loss, as restated for 2007	\$ (2,534)	\$ (3,747)
Net impact of foreign currency translation adjustments – gain (loss)	<u>(606)</u>	<u>375</u>
Comprehensive loss	<u>\$ (3,140)</u>	<u>\$ (3,372)</u>

Advertising

Advertising costs are expensed as incurred and amounted to \$635 and \$197 and \$641 for the years ended January 31, 2009 and 2008, respectively.

3. Summary of Significant Accounting Policies (continued)

Shipping and Handling Revenues and Costs

Fees billed to customers associated with shipping and handling activities are classified as revenue, and costs associated with shipping and handling are classified as part of cost of sales.

Concentration Risk

The Company has bank deposits in excess of federal deposit insurance.

API has five suppliers from whom approximately 40% and 37% of its total purchases were made during the years ended January 31, 2009 and 2008, respectively. Accounts payable to these vendors totaled \$1,432 and \$2,524 at January 31, 2009 and 2008, respectively.

Share-Based Payments

The Company has certain stock-based compensation as more fully described in Note 7, which is accounted for in accordance with SFAS No. 123(R), *Share-Based Payment*.

Compensation expense (based upon the fair value on the date of grant) is recognized in the consolidated statement of operations over the requisite service period, which for the Company is generally the vesting period, for all new awards and unvested awards that are expected to vest over the service period.

Fair Value Measurements

SFAS No. 157, *Fair Value Measurements*, was adopted by the Company effective on February 1, 2008. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. The FASB approved a one-year deferral of the adoption of SFAS No. 157 as it relates to nonfinancial assets and liabilities measured at fair value on a nonrecurring basis with the issuance in February 2008 of FASB Staff Position FAS 157-2, *Effective Date of FASB Statement No. 157*, as a result of which implementation by the Company is now required for the year ended January 31, 2010. The partial adoption of SFAS No. 157 for the year ended January 31, 2009 had no impact on the Company's consolidated financial statements. The Company is in the process of evaluating SFAS No. 157 as it relates to nonfinancial assets and liabilities but does not believe it will have an impact on the consolidated financial statements.

SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*, was adopted by the Company effective on February 1, 2008. SFAS No. 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The adoption of SFAS No. 159 did not have any impact on the Company's consolidated financial statements.

3. Summary of Significant Accounting Policies (continued)

Fair Value Measurements (continued)

The carrying values of current assets and liabilities approximate fair value due to the short-term maturities of these assets and liabilities. The carrying amount of the Company's borrowings under its debt agreements approximates fair value, as these obligations have interest rates which vary in conjunction with current market conditions.

Reclassifications

Certain amounts have been reclassified to conform to the current year presentation. The effect of the reclassifications did not impact the consolidated financial position or results of operations.

New Accounting Standards

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations*. SFAS No. 141(R) seeks to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a business combination and its effects. SFAS No. 141(R) requires an acquirer to recognize the assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date, measured at their fair values as of that date, with limited exceptions. This standard also requires the acquirer in a business combination achieved in stages to recognize the identifiable assets and liabilities, as well as the noncontrolling interest in the acquiree, at the full amounts of their fair values. SFAS No. 141(R) requires an acquirer to recognize adjustments made during the measurement period to the acquired assets and liabilities as if they had occurred on the acquisition date and revise prior period financial statements in subsequent filings for changes. In addition, SFAS No. 141(R) requires that all acquisition related costs be expensed as incurred, rather than capitalized as part of the purchase price and those restructuring costs that an acquirer expected but was not obligated to incur to be recognized separately from the business combination. SFAS No. 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. The Company will adopt SFAS No. 141(R) on February 1, 2009 prospectively.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements—an amendment of ARB No. 51*. SFAS No. 160 amends Accounting Research Bulletin ("ARB") No. 51 to establish accounting and reporting standards for the noncontrolling (minority) interest in a subsidiary and for the deconsolidation of a subsidiary. It clarifies that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the financial statements. SFAS No. 160 also requires net income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest on the face of the statement of operations. Under SFAS No. 160, the accounting for changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation must be accounted for as equity transactions for the difference between the parent's carrying value and the

3. Summary of Significant Accounting Policies (continued)

New Accounting Standards (continued)

cash exchanged in the transaction. In addition, SFAS No. 160 also requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated (except in the case of a spin-off), and requires expanded disclosures in the consolidated financial statements that clearly identify and distinguish between the interests of the parent's ownership interest and the interests of the noncontrolling owners of a subsidiary. SFAS No. 160 is effective for fiscal years, beginning on or after December 15, 2008. The Company will adopt SFAS No. 160 on February 1, 2009 prospectively. The Company does not expect the adoption of the provisions of SFAS No. 160 to have a material impact on the Company's consolidated financial statements.

4. Plant and Equipment

Plant and equipment consist of the following:

	<u>2009</u>	<u>2008</u>
Machinery and equipment	\$ 2,434	\$ 2,431
Buildings and leasehold improvements	1,051	1,051
Computer equipment, software, office furniture, fixtures and other office equipment	12,814	12,153
Construction-in-process	<u>56</u>	<u>63</u>
	16,355	15,698
Less: accumulated depreciation	<u>(13,102)</u>	<u>(11,634)</u>
	<u>\$ 3,253</u>	<u>\$ 4,064</u>

The amount of the unamortized capitalized software at January 31, 2009 and 2008 was \$1,750 and \$2,506, respectively. The related amortization expense during the years ended January 31, 2009 and 2008 was \$887 and \$983, respectively. The Company changed its estimate of the remaining useful life of its enterprise software during the year ended January 31, 2009, which decreased amortization expense by \$121.

5. Revolving Line of Credit and JEM III LLC Subordinated Debt

	<u>2009</u>	<u>2008</u>
Revolving line of credit	\$ 20,706	\$ 20,374
Subordinated debt	<u>2,000</u>	<u>2,000</u>
	<u>\$ 22,706</u>	<u>\$ 22,374</u>

On November 2, 2007, the Company entered into a Master Affirmation and Second Amendment to Loan Documents (the "Second Amendment") with TD Banknorth, NA, which amends the second Amended and Restated Loan and Security Agreement (the "Agreement") dated January 11, 2007, a \$25,000 revolving credit facility, which was set to expire on September 1, 2008. The Second Amendment provides for a 36-month senior revolving credit facility (the "Revolving Loan Facility")

5. Revolving Line of Credit and JEM III LLC Subordinated Debt (continued)

in the amount of \$32,000, subject to a borrowing base based on a formula of qualifying assets as well as outstanding letters of credit, and expires on September 1, 2010. The proceeds of any loans made under the Revolving Loan Facility will be used for working capital purposes in the ordinary course of business. Changes to the debt service coverage ratios and interest rate pricing were also modified as a result of the Second Amendment.

On May 19, 2008, the Company entered into a Master Affirmation and Third Amendment to Loan Documents (the "Third Amendment") with TD Banknorth, NA, which amends the Agreement by providing: a waiver of certain covenant defaults for the periods ended October 31, 2007 and January 31, 2008; an amendment to certain covenants; and the ability by borrower to use up to \$500 of the Revolving Credit Facility to finance redemption of equity interests.

On October 23, 2009, the Company entered into a Master Reaffirmation and Fourth Amendment to Loan Documents (the "Fourth Amendment") with TD Bank, N.A., formerly known as TD Banknorth, N.A, which amends the Agreement by providing: a waiver of certain covenant defaults for the periods ended January 31, 2009 and April 30, 2009; and an amendment to certain covenants.

The Revolving Loan Facility bears interest at the option of the borrower (i) at the prime rate in effect from time to time, (ii) at the adjusted LIBOR for the applicable interest period plus 150, 175, 200, or 225 basis points depending upon financial ratios of the borrower, or (iii) at the FHLB Rate (the "Federal Home Loan Bank Rate"). Effective July 1, 2009, the interest rate changed to adjusted LIBOR (as defined) plus 450 basis points. The Agreement contains numerous covenants, including restrictions on mergers, consolidations and acquisitions, the incurrence of indebtedness, transactions with affiliates, the creation of liens, and limitations on capital expenditures. Pursuant to the terms and conditions of the Agreement, the payment of dividends on the Company's common stock is prohibited, except with the lender's consent, and the Company is required to maintain minimum levels of Tangible Capital Base and specified Debt Service Coverage. Substantially all of the Company's domestic and Canadian assets are pledged as collateral under the Agreement, and the Company guarantees all borrowings under the Agreement.

The entire Revolving Loan Facility is classified as current debt based upon the subjective acceleration clause and required lockbox cash management agreement.

JEM III LLC, a related party, provided a loan to the Company up to \$5,000 to fund operations. The Company borrowed \$3,000 during the year ended January 31, 2008. This note matures on the same date (September 1, 2010) and is subordinate to the Revolving Loan Facility in that one of the following conditions must be met in order for payment to be made: (i) written consent from TD Banknorth, NA, (ii) the Revolving Loan Facility has been repaid in full and the Agreement terminated, or (iii) the Revolving Loan Facility is not in default and the proposed payment does not exceed the availability on the Revolving Loan Facility plus \$500. As a requirement of the Second Amendment, \$1,000 was repaid upon execution of the Amendment. Interest on the subordinated debt is at LIBOR plus 500 basis points (paid through September 2007). Accrued interest payable at January 31, 2009 and 2008 is \$247 and \$130, respectively.

6. Note Payable

	<u>2009</u>	<u>2008</u>
Note payable	\$ 537	\$ 1,042
Less: current portion	<u>(537)</u>	<u>(598)</u>
Long-term portion	<u>\$ -</u>	<u>\$ 444</u>

API entered into an initial parts purchase agreement on September 20, 2005, with a leading aircraft original equipment manufacturer ("OEM") to purchase inventory and sell parts. The promissory note is for a term of 4 years, at 5.0% interest per annum payable quarterly through 2010. The promissory note is subordinated to the Company's Revolving Line Facility.

7. Share-Based Payments

The Company has a Stock Incentive Plan (the "Plan") with a total of 1,200,000 shares of common stock reserved for issuance. The Plan provides for the grant of incentive stock options, nonqualified stock options, stock appreciation rights, stock grants and stock purchase rights. At January 31, 2009, 626,439 shares (after forfeitures) have been issued under the Plan.

The Company's non-employee directors receive a portion of their annual compensation in the Company's stock. The value of stock issued is equivalent to the compensation expense, and the number of shares issued is based upon the fair value per share at the date issued. The Company's non-employee directors receive compensation in cash for committee meetings and special board meetings, excluding the four regularly scheduled board meetings and the annual shareholders' meeting that are paid for in stock as part of their annual compensation.

Compensation expense related to non-employee directors totaled \$86 and \$75, and the number of shares issued was 77,634 and 43,074 for the years ended January 31, 2009 and 2008, respectively. A total of 35,010 and 318,979 shares have been issued to directors under the Plan.

The Company has issued restricted stock awards to its President as follows:

	<u>2009</u>		<u>2008</u>	
	<u>Number of Shares</u>	<u>Grant Date Fair Value</u>	<u>Number of Shares</u>	<u>Grant Date Fair Value</u>
Outstanding (nonvested) at beginning of year	56,385	\$ 2.17	-	\$ 2.17
Granted	-	-	70,000	-
Vested	<u>(23,340)</u>	<u>2.17</u>	<u>(13,615)</u>	<u>2.17</u>
Outstanding (nonvested) at end of year	<u>33,045</u>	<u>\$ 2.17</u>	<u>56,385</u>	<u>\$ 2.17</u>

Compensation expense related to the restricted stock awards totaled \$51 and \$30, and the number of shares issued was 35,010 and -0- for the years ended January 31, 2009 and 2008.

7. Share-Based Payments (continued)

As of January 31, 2009, \$72 of unrecognized cost related to nonvested restricted stock awards is expected to be recognized over a weighted average period of approximately 1.4 years.

The Company generally grants stock options to its employees for a fixed number of shares with an exercise price equal to the fair value of the stock on the date of grant. The fair value of the stock options granted was estimated at the date of grant using a Black-Scholes option-pricing model beginning on February 1, 2006.

The fair value of each option granted was estimated at the date of grant using the following assumptions for the years ended January 31, 2009 and 2008:

	<u>2009</u>	<u>2008</u>
Expected dividend yield	0.0%	0.0%
Risk-free interest rate	2.9%	4.7%
Expected volatility	33.0%	33.0%
Expected life of option	5 years	5 years
Weighted average fair value of options granted during the year	\$.51	\$.86

All of the stock options vest ratably over two to five-year periods, beginning one year after the date of the grant, and expire ten years after issuance. The following table is a summary of activity related to stock options for the years ended January 31, 2009 and 2008:

	<u>2009</u>		<u>2008</u>	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
Outstanding at beginning of year	132,150	\$ 3.32	77,150	\$ 4.44
Granted	15,000	1.50	80,000	2.49
Exercised	-	-	-	-
Forfeited	(35,500)	4.63	(25,000)	4.12
Outstanding at end of year	<u>111,650</u>	<u>\$ 2.66</u>	<u>132,150</u>	<u>\$ 3.32</u>
Exercisable at end of year	<u>43,317</u>	<u>\$ 3.25</u>	<u>52,150</u>	<u>\$ 4.58</u>

The aggregate intrinsic value of options outstanding and exercisable at January 31, 2009, was \$-0-.

The weighted average remaining contractual term of options outstanding and exercisable at January 31, 2009, is 4 years.

7. Share-Based Payments (continued)

	<u>2009</u>		<u>2008</u>	
	<u>Number of Options</u>	<u>Weighted Average Exercise Price</u>	<u>Number of Options</u>	<u>Weighted Average Exercise Price</u>
Nonvested at beginning of the year	80,000	\$ 2.49	17,882	\$ 4.25
Granted	15,000	1.50	80,000	2.49
Vested	(26,667)	4.25	(6,215)	4.25
Forfeited	-	4.63	(11,667)	4.25
Nonvested at end of the year	<u>68,333</u>	<u>\$ 4.91</u>	<u>80,000</u>	<u>\$ 2.49</u>

As of January 31, 2009, \$44 of unrecognized compensation cost related to nonvested stock options is expected to be recognized over a weighted average period of approximately 1.6 years.

The Company has an Employee Stock Purchase Plan ("ESPP"). Under the ESPP, 250,000 shares of common stock have been reserved for issuance. With certain limitations, the ESPP allows for eligible employees to purchase stock through payroll deductions at 85% of the lower of the fair value of the Company's common stock as of the first day of each semi-annual offering period or the fair market value of the stock at the end of the offering period. The Company did not issue any shares of stock under the ESPP during the years ended January 31, 2009 and 2008. At January 31, 2009, 173,955 shares were available to be issued under the ESPP.

8. Stock Repurchase Program

In a series of authorizations commencing November 3, 1999, the Company's Board of Directors authorized a repurchase program of up to 2,118,817 shares of the Company's common stock. The repurchases have been funded from a portion of the proceeds from the sale of its previously owned subsidiary National Airmotive Corp., and were made from time to time in open market transactions, block purchases, privately negotiated transactions or otherwise at prices prevailing at the time of the repurchase. The aggregate share repurchases since the repurchase program began totaled 2,024,498 shares through January 31, 2002, at an aggregate cost of \$10,708 or \$5.29 per share. There have been no repurchases since that time. Approximately 94,000 shares remain available for repurchase under this program.

9. Income Taxes

The (provision) benefit for income taxes on continuing operations is as follows:

	<u>2009</u>	<u>2008</u>
Current:		
Federal and foreign	\$ -	\$ -
State	-	-
	<u>-</u>	<u>-</u>
Deferred:		
Federal and foreign	\$ -	\$ -
State	-	-
	<u>-</u>	<u>-</u>
Total (provision) benefit	<u>\$ -</u>	<u>\$ -</u>

The Company's effective rate is as follows:

	<u>2009</u>	<u>2008</u>
Federal statutory rate	34.0%	34.0%
State taxes, net of federal	-	-
Foreign tax provision, net of federal	-	-
Net operating loss utilized	-	-
Non-deductible items	(1.7)	(.7)
Prior year and other items	-	(.2)
Adjustments to tax liabilities	-	-
Deferred tax valuation allowance	<u>(32.3)</u>	<u>(33.1)</u>
	<u>-</u>	<u>-</u>

The Company's net deferred tax asset is as follows:

	<u>2009</u>	<u>2008</u>
Deferred tax assets (liabilities):		
Bad debts	\$ 458	\$ 362
Inventory reserve	1,558	1,973
Amortization of tax goodwill	694	650
Net operating loss carryforwards	8,837	6,198
Other	<u>158</u>	<u>59</u>
	11,705	9,242
Valuation allowance	<u>\$ (11,705)</u>	<u>\$ (9,242)</u>
Net deferred income tax asset	<u>\$ -</u>	<u>\$ -</u>

9. Income Taxes (continued)

The Company has net operating loss carryforwards totaling approximately \$24,279 for federal income tax purposes, and various state net operating loss carryforwards. The carryforwards expire between 2023 and 2029. The Company's valuation allowance was increased \$2,463 and \$1,004 for the years ended January 31, 2009 and 2008, respectively.

The Company files income tax returns in the U.S., various U.S. states and certain foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examination for years through 2005. There are no current examinations in any income tax jurisdiction.

10. Employee Benefit Plan

API maintains a defined contribution savings plan, qualified under Section 401(k) of the Internal Revenue Code that covers substantially all of its full-time employees. The savings plan allows employees to defer up to 15% of their salary, with the Company partially matching employee contributions. Effective February 1, 2009, the Company suspended matching contributions. Employees vest in the Company contribution ratably over three years. The Company expensed \$118 and \$148 related to the savings plan during the years ended January 31, 2009 and 2008, respectively. Employees do not have an option to invest in the Company's stock under the savings plan.

11. Related Party Transactions

The Company and First Equity Development, Inc. ("First Equity") the wholly-owned subsidiary of First Equity Group, Inc., the majority stockholder of the Company, have an agreement relating to the allocation of potential investment and acquisition opportunities in the aerospace parts distribution and logistics businesses. The agreement was approved by the independent members of the Board of Directors on a month-to-month basis effective February 1, 2004. First Equity Group, Inc. is beneficially owned by Mr. Aaron P. Hollander and Mr. Michael C. Culver, President and Chief Executive Officer and former Vice Chairman of the Company, respectively. Pursuant to the agreement, neither First Equity nor any of its majority-owned subsidiaries will consummate any acquisition of a majority interest in any aerospace parts distributions and logistics business anywhere in the world (a "Covered Acquisition"), without first notifying the Company and providing the Company with the opportunity to effect the Covered Acquisition for its own account. The Company's decision as to whether to effect the Covered Acquisition will be made by the independent members of the Board of Directors of the Company. The agreement can be terminated by either party upon 30 days written notice to the other party. The agreement does not apply to any proposed acquisition by First Equity of any business that generates less than 15% of its aggregate net sales from aerospace parts distribution or logistics, or to any advisory services performed by First Equity on behalf of third parties.

11. Related Party Transactions (continued)

The Company subleases from First Equity office space in Westport, CT. The leased space is utilized by the Company as its corporate headquarters. First Equity also utilizes space in the same premises. The sublease, which became effective April 21, 1997, is for a period of ten years, and is cancelable by either party with six months notice. First Equity has renewed the lease for an additional five-year period beginning in April 2007. Lease payments under this sublease totaled approximately \$51 and \$89, for the years ended January 31, 2009 and 2008, respectively.

The Company and First Equity also share certain common expenses that arise from sharing office space in Westport, CT. The Company reimburses First Equity and vice versa, for expenses each entity incurs related to the common usage of the office space. The amounts are included in the Company's corporate expenses, and include expenses such as telephone, computer consulting, office cleaning, office supplies and utilities. The expenses are allocated based upon a formula reviewed and approved by the independent directors of the Company. Management believes this method of allocation is reasonable. In addition, the amounts reimbursed by the Company are the actual costs incurred for the expense. The Company reimbursed First Equity, \$31 and \$36 in 2009 and 2008, respectively.

In order to simplify the administration of payroll, certain employees of the Company who are authorized to perform services for both the Company and First Equity are paid through the payroll of First Equity. Employees of the Company who work exclusively for the Company by agreement are paid through the payroll of API, the Company's principal subsidiary.

12. Interest Expense and Other Income, Net

	<u>Year ended January 31,</u>	
	<u>2009</u>	<u>2008</u>
Interest expense	\$ (1,421)	\$ (1,957)
Foreign exchange gain	41	539
Other income	<u>6</u>	<u>19</u>
	<u>\$ (1,374)</u>	<u>\$ (1,399)</u>

The components primarily relate to interest expense on debt and foreign exchange transaction gain from Canadian functional currency (API Ltd.). Effective February 1, 2008 the Company's Board of Directors authorized that \$2,000 of intercompany debt from API Ltd. to API be considered as "long-term investment" and, as such, foreign exchange transaction adjustments are included in Other Comprehensive Income (reported in Stockholders' Equity).

13. Net Loss Per Share

The following sets forth the denominator used in the computation of basic earnings per share and earnings per share - assuming dilution.

	<u>Year ended January 31,</u>	
	<u>2009</u>	<u>2008</u>
Denominator for basic net income (loss) per share – weighted average shares	7,465,583	7,409,332
Effect of dilutive employee stock options	<u>-</u>	<u>-</u>
Denominator for net income (loss) per share – assuming dilution – adjusted weighted average shares and assumed conversions	<u>7,465,583</u>	<u>7,409,332</u>

Stock options (Note 7) are not considered in the loss per share computations as the effects would be anti-dilutive.

14. Commitments and Contingencies

Commitments

The Company leases certain warehouse facilities, equipment and office space. Certain of the Company's operating leases have options which allow the Company, at the end of the initial lease term, to renew the leases for periods ranging from three to five years. Certain leases also allow for cancellation of the lease upon payment of a penalty. Certain lease agreements also contain escalation clauses that are based on the consumer price index. Future minimum rental payments under operating leases that have initial noncancelable lease terms in excess of one year as of January 31, 2009, are as follows:

2010	\$ 1,276
2011	1,211
2012	1,180
2013	1,190
2014	685
Thereafter	<u>1,425</u>
Total	<u>\$ 6,967</u>

Rental expense under noncancelable operating leases amounted to \$1,515 and \$1,531 for the years ended January 31, 2009 and 2008.

14. Commitments and Contingencies (continued)

Contingencies

In the ordinary course of business, the Company is subject to many levels of governmental inquiry and investigation. Among the agencies that oversee the Company's business activities are the Federal Aviation Administration, the Department of Transportation and the Environmental Protection Agency. The Company does not anticipate that any action as a result of such inquiries and investigations would have a material adverse affect on its consolidated financial position, results of operations, cash flows or its ability to conduct business.

In the normal conduct of its business, the Company also is involved in various claims and lawsuits, none of which, in the opinion of the Company's management, will have a material adverse impact on the Company's consolidated financial position, results of operations or cash flows. The Company maintains what it believes is adequate liability and other insurance to protect it from such claims.