

AeroMechanical Services Ltd.

2009 Annual Report

TSX.V: AMA

F L **Y** H T™

AeroMechanical Services Ltd.



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Introduction

AeroMechanical Services Ltd. (the “Company” or “AMA”) provides proprietary technological solutions and services designed to reduce costs and improve efficiencies in the aviation industry. The Company has successfully commercialized three products and associated services currently marketed to airlines, manufacturers, and maintenance organizations around the world. Its technologies, afirs UpTime, FIRST, and FLYHT Fuel Management System enable airlines to monitor and manage aircraft operations anywhere, anytime, in real-time.

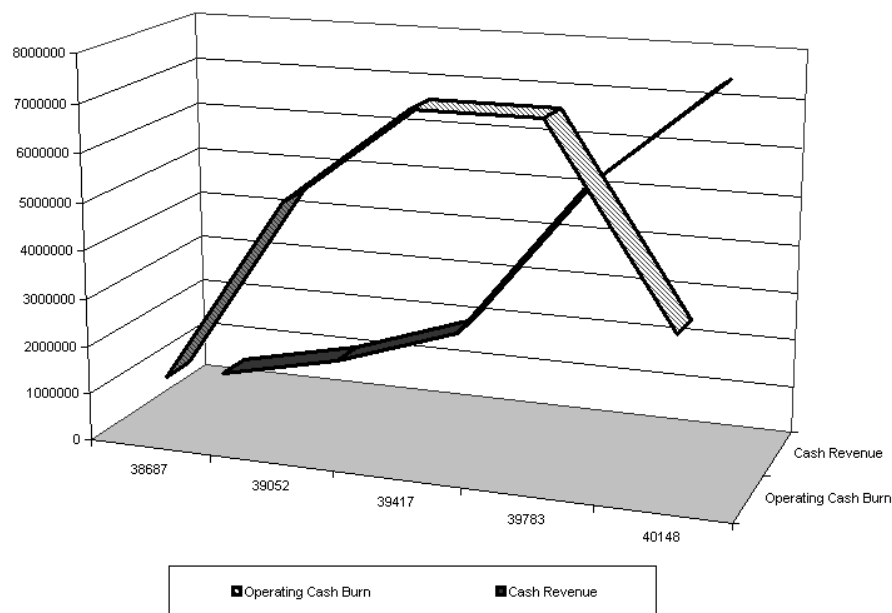
AeroMechanical was founded in 1998 and has been publicly traded on the Toronto Venture Exchange (TSX.V: AMA) since March 2003. The Company's solutions and services are primarily sold under the FLYHT brand name.

Letter to the Shareholders

To Our Shareholders,

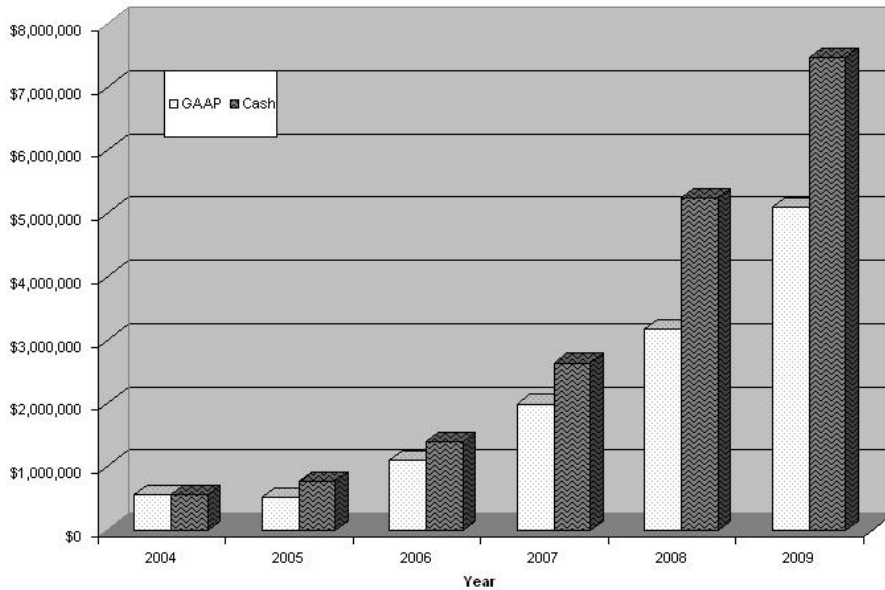
I am sure that every one of you is as relieved to have 2009 behind us as we ourselves are. It was one of those years for the record books but in the face of many obstacles, we were able to make some headway. During the year we continued our growth in revenue, closing 2009 60% ahead of 2008. While we didn't quite make our goal of 100% growth, year over year, given the challenges in our market space, we are quite pleased with the performance. Since we had cleared up nearly all of our backlog by the end of the year, and new sales were scarce last year, Q4 was a bit of an off quarter. However, expectations are high that we are going to build our backlog significantly due to deals that were signed in 2009. We cannot overemphasize the importance of the L-3 Communications ("L3") teaming agreement signed in November of last year in giving us a recognized presence in the global aviation market. L-3 is a very large and respected supplier to airline manufacturers around the globe, and being selected as their partner in improving the performance characteristics of the "black box" is a real feather in our cap. That and the continued support of Sierra Nevada Corporation in completing the next generation of afirs for deployment, has put us in good stead in the aviation communication services markets we intend to serve for the next decade and beyond. Additionally, along with the continued efforts of the Meggitt PLC team and our sales team, our efforts will hopefully bear fruit with Original Equipment Manufacturers ("OEMs") in 2010. We were successful in our first OEM installation with Hawker Beech this summer, but the slowdown in business aviation has also slowed our efforts in that market.

During 2009 we invested in our new products, growing and stabilizing our staff, and making sure we were poised for growth as the global economy comes out of the tailspin it has been in. During the year we reduced our expenses by nearly \$2 million while growing our revenues by nearly \$2 million. That \$4 million is reflected in the \$0.06 per share loss, down from \$0.11 one year ago.



While the jury is still out on 2010 and beyond, early indications are that the aviation industry is poised for a slow recovery. We have announced a couple of significant deals this year that are a culmination of a lot of work by our team over the last couple of years. Our diligence in the marketplace is being rewarded and our industry leading technologies such as the FLYHTStream product to get real-time black box data to the ground, FUEL products to help reduce greenhouse gas emissions, and the afirs 228 to meet emerging air traffic control rules continue to provide results for our customers as they roll out in the US, Europe, and beyond. We have strengthened our balance sheet and are poised to deliver superior products to customers as they emerge from the recession. Despite the slowed economy, our customers survived and in some cases thrived. That is reflected in our continued revenue growth.

Revenue History - All Products & Services



We want to thank our shareholders for their patience, our staff for their dedication and efforts, and our board of directors for their unwavering support as we navigate the uncertainties of the global economy.

Yours truly,

William Tempany

Chief Executive Officer

Market Overview

The pace of economic slowdown during the year was faster than most had predicted. What had first been expected to be a downturn in key developed economies turned into a global recession in the autumn of 2008. With record oil and commodity prices, commodities collapsing, and an unprecedented financial crisis all striking at once, even those emerging economies that had been expected to go untouched by recession saw sharp declines in growth.

Globally, growth began slowing in the first half of the year, soon after the US economy went into recession in the last quarter of 2008. In all economies, consumer and business confidence plummeted due to rising unemployment, uncertainty in the capital markets, a continuing squeeze on credit, the erosion of household budgets, and falling house prices. Growth also slowed dramatically in many Asian economies.

Government attempts – nationally and internationally – to halt the financial crisis through bank bailouts and credit guarantees staved off what might have been an even more serious collapse. Subsequent efforts to stimulate economic activity are expected by most economists to take longer to take effect.

It is hoped that these steps will kick-start the US and UK economies, which will provide some economic growth in 2010. This should, in turn, provide some basis for a recovery in our customers' businesses.

Impact on the Industry

The airline industry acts as an economic barometer. Airlines feel the full force of falling confidence quickly and, on this occasion, dramatically. During the first half of 2008, oil prices hit a record high of \$146 a barrel, forcing up the fuel costs of all carriers to unprecedented levels and putting margins under enormous pressure. Although fuel prices subsequently fell to about a third of that level, the onset of recession had already begun in earnest, forcing many airlines into financial loss.

Even at these lower levels, fuel remains a much bigger proportion of airline costs compared to a few years ago, and the prospect of renewed volatility in prices remains a long-term concern.

From information available on the internet the most significant impact of the downturn has been on premium passengers, with businesses looking to cut back sharply on travel to save money. IATA's latest available figures show that global premium traffic fell in 2008 by 2.8 percent. The rate of decline is increasing, and IATA has indicated that in the first three months of 2009 it was around 19 percent. The rate of decline varied across the world, with trans-Pacific traffic and routes within Asia most severely hit. There was also a decrease in air freight traffic, although not nearly as catastrophic as that of ocean freight transport. The recovery has started, and the IATA figures show slow growth in most major markets for 2010 and beyond.

Air Freight is Learning its Lessons and Becoming a Different Industry

The massive decline in international air freight traffic due to the global recession—over 20% year-on-year at the lowest point—has given way to the first signs of recovery. But cargo will likely never again experience “business as usual”.

IATA expects 2009 to show a 13% contraction, with a modest improvement of 7.7% in 2010. Total freight volumes will remain 10% below the 41.8 million tonne peak recorded in 2007, although cargo demand is rising slightly faster than world trade as companies look to replenish inventories. Yields have been hit hard, last year plummeting 15%. They are expected to only improve by 0.9% in 2010.

And even though marginally better times may be on the horizon, a cautious attitude to the figures is still advised. Brian Pearce, IATA Chief Economist, stresses that air freight has so far only recovered about half of the volumes lost in 2008.

“There are headwinds to any growth,” he says. “Banks are still short of capital, high unemployment effects will come into play, and consumer debt is high—it’s 130% of annual income in the US. This affects spending patterns and will ripple through the system. Another factor is the unevenness of growth,” he continues. “There is only a small increase in demand in developed nations compared with the likes of India, China, and Brazil.”

Freight Carriers Hard Hit as Well

Changes in the cargo environment have both external and internal drivers. Externally, issues such as the fuel price will continue to be a significant variable, capable of great impact. An average oil price of \$75 per barrel (Brent) is expected in 2010, up from the \$61.8 average in 2009.

This challenge is shared with the passenger sector, and cargo will similarly find the solution in better fuel management, such as operational efficiency and new aircraft.

Fuel is Becoming the Watchword Again

As this chart shows, the return of more robust economies around the world will herald the return of rising energy prices. We are already seeing prices that exceed the prices pre-2008 run up and there are not signs that this trend will not continue.



We have continued to develop our Fuel system capabilities, and more airlines are turning their attention back to the cost of fuel since the normalization of their fleets, routes, and schedules to the new economic realities has been completed. This inevitable rise in costs will be a harbinger of good things for AMA as we have tools that will allow airlines to actively monitor standard operating procedures for compliance and save money by effectively communicating with and training personnel on the proper use of this valuable commodity.

Solutions & Services

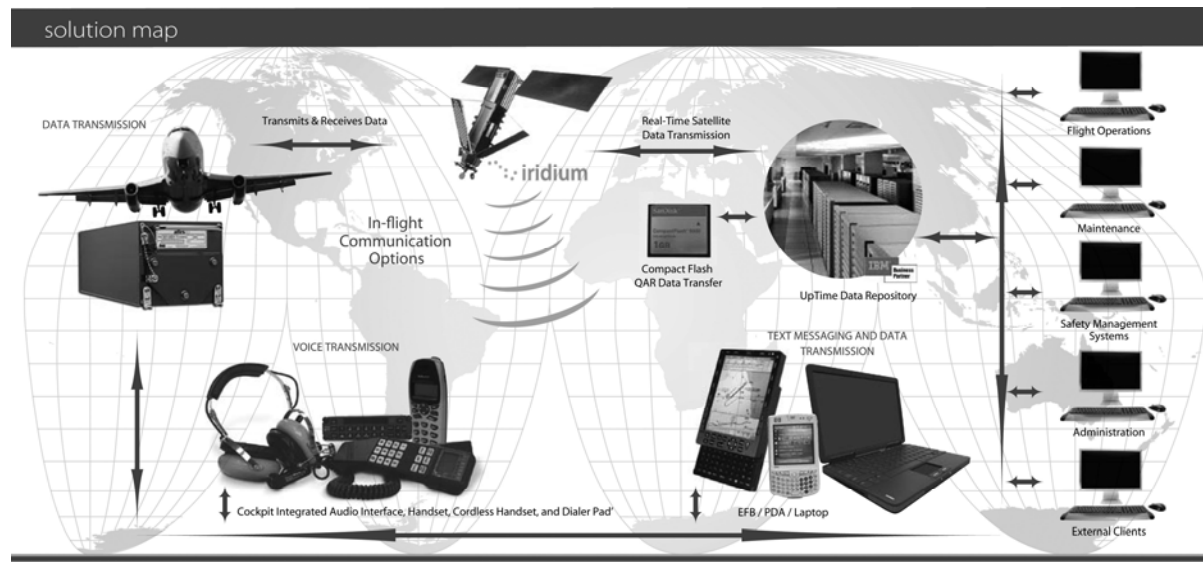
AMA's solutions and services are proudly marketed and sold under the FLYHT brand name. The Company provides innovative value added data and consulting solutions designed to improve profitability and efficiency within the aerospace industry.

afirs UpTime

afirs UpTime is a satellite-based Automated Flight Information Reporting System ("afirs") that allows aircraft operators to manage and monitor aircraft operations anywhere, anytime, in real-time.

The afirs unit is an avionics component that resides on the aircraft. The afirs unit monitors the various systems on the aircraft, and when certain events are detected information is transmitted via Iridium satellite.

The afirs unit also provides satellite phone capabilities and connectivity to a laptop computer in the cockpit allowing aircrew to make phone calls, request weather reports, and send messages to the ground. UpTime is the ground-based database that receives the information, stores it, and creates reports for customers.



FIRST

The Fuel Initiative Reporting System Tracker ("FIRST") provides a tool to eliminate uncertainty about the effectiveness of an airline's fuel savings initiatives. FIRST can be purchased separately as a standalone module from the Fuel Management System. It uses real-time flight data acquired from the aircraft onboard systems, and presents the data to operations personnel in an easy to read dashboard that displays the level of compliance with flight operations pilot initiatives for fuel conservation. Where compliance has not been met, costs are shown. **Experience with this tool at airlines has shown conservative opportunities for savings of \$50 USD per flight, \$80 USD per**

flight when used with afirs data. Airlines interested in this tool fly between 20,000 to 50,000 hours annually. This tool is de-identified to meet pilot union requirements, but can be filtered to display performance by pilot if desired.

FLYHT Fuel Management System

The FLYHT Fuel Management System is a powerful way to focus attention on the areas of greatest savings potential automatically, and to provide the information necessary to make decisions about the operation. Most airlines currently rely on a system of reports, manually generated and analyzed to make fuel savings decisions within the operation. This is time consuming and relies on the user to “figure out” where the areas of potential are by cross-referencing a great number of queries. The FLYHT Fuel Management System is not just a report generation tool, it is a dynamic, interactive application that answers key questions by generating alerts and providing the user the ability to quickly identify trends. FLYHT teamed up with an award winning user experience development team to design this unique application that highlights exceptions to best practices, provides quick drill downs to spot the root cause, and identifies trends. It is an intuitive tool that gets fuel managers acting on information instead of compiling and analyzing data.

The Fuel Management System is ideally suited for large commercial airlines and is designed to receive inputs from afirs[™], ACARS, Flight Planning Systems, Load Planning Systems, and Electronic Flight Bags (EFBs). The system can also operate independently of afirs.

Fuel Evaluation

The Fuel Evaluation is a consulting engagement with our team of experts who evaluate an airline’s operations and develops recommendations to reduce fuel consumption and CO₂ emissions. The team is comprised of industry experts in the fields of flight operations, dispatch and operations control, and maintenance and engineering. They have experience with fleet sizes ranging from 2 to 300+ aircraft including all Boeing, Airbus, and regional aircraft manufacturers’ models.



Management Discussion & Analysis

This management discussion and analysis (“MD&A”) should be read in conjunction with the audited annual consolidated financial statements of AeroMechanical Services Ltd. (“AMA” or the “Company”) as at and for the years ended December 31, 2009 and 2008. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”). Additional information with respect to AMA can be found on SEDAR at www.sedar.com.

This MD&A is dated April 19, 2010.

Non-GAAP Financial Measures

The Company reports its financial results in accordance with GAAP. It also occasionally uses certain non-GAAP financial measures, such as working capital, modified working capital, and cash revenue. AMA defines working capital as current assets less current liabilities. The Company defines modified working capital as current assets less current liabilities, not including customer deposits or the current portion of unearned revenue because those customer deposits are non-refundable. AMA defines cash revenue as financial statement revenue plus arrangement consideration received during the period that has not yet been recognized as revenue in the period. These non-GAAP financial measures are always clearly indicated. The Company believes that these non-GAAP financial measures provide investors and analysts with useful information so they can better understand the financial results and perform a better analysis of the Company’s growth and profitability potential. Since non-GAAP financial measures do not have a standardized definition, they may differ from the non-GAAP financial measures used by other companies. The Company strongly encourages investors to review its financial statements and other publicly filed reports in their entirety and not rely on a single non-GAAP measure.

Forward-Looking Statements

This discussion includes certain statements that may be deemed “forward-looking statements” that are subject to risks and uncertainty. All statements, other than statements of historical facts included in this discussion, including, without limitation, those regarding the Company’s financial position, business strategy, projected costs, future plans, projected revenues, objectives of management for future operations, the Company’s ability to meet any repayment obligations, the use of non-GAAP financial measures, trends in the airline industry, the global financial outlook, expanding markets, research and development of next generation products and any government assistance in financing such developments, foreign exchange rate outlooks, new revenue streams and sales projections, cost increases as related to marketing, research and development, administration expenses, and litigation matters, may be or include forward-looking statements. Although the Company believes the expectations expressed in such forward-looking statements are based on a number of reasonable assumptions regarding the Canadian, U.S., and global economic environments, local and foreign government policies/regulations and actions and assumptions made based upon discussions to date with the Company’s customers and advisers, such statements are not guarantees of future performance and actual results or developments may differ materially from those in the forward-looking statements. Factors that could cause actual results to differ materially from those in the

forward-looking statements include production rates, timing for product deliveries and installations, Canadian, U.S., and foreign government activities, volatility of the aviation market for the Company's products and services, factors that result in significant and prolonged disruption of air travel worldwide, U.S. military activity, market prices, foreign exchange rates, continued availability of capital and financing and general economic, market, or business conditions in the aviation industry, worldwide political stability or any effect those may have on our customer base. Investors are cautioned that any such statements are not guarantees of future performance and that actual results or developments may differ materially from those projected in the forward-looking statements.

Although the Company believes that the expectations reflected in such forward-looking statements are reasonable, there can be no assurance that such expectations will prove to have been correct. The Company cannot assure investors that actual results will be consistent with any forward-looking statements; accordingly, readers should not place undue reliance on forward-looking statements. The forward-looking statements contained herein are current only as of the date of this document. The Company disclaims any intentions or obligation to update or revise any forward-looking statements or comments as a result of any new information, future event or otherwise, unless such disclosure is required by law.

Overview

AeroMechanical Services Ltd. is a designer, developer, and service provider of innovative solutions to the global aerospace industry. The Company's solutions are designed to improve the productivity and profitability of our customers and to ensure that the communications between terrestrial and airborne staff and assets is to the highest possible standard. Our tools also provide the ability to deliver large amounts of data if an aircraft is in distress through our FLYHTStream product.

The major products of the Company are the Automated Flight Information Reporting System ("afirs"), UpTime, Fuel Initiative Reporting System Tracker ("FIRST"), FLYHT Fuel Management System, Underfloor Stowage Unit, FLYHTStream, and AeroQ. These products are marketed globally by a team of several employees and agents based in Canada, United States, United Kingdom, France, Switzerland, Abu Dhabi, Ireland, and Argentina. A Calgary employee is currently spending more than 95% of his time in China working on opportunities there.

In 2009 AMA continued on the progress made in 2008 through an increase in recurring revenues of afirs UpTime and services revenue. This progress with these two revenue streams continues to further define AMA as an aviation solutions company. The continued research and development of our leading edge technology and services and the development of add-on products such as FIRST, FuelMI, and FLYHTStream is being transformed into a continuous telecommunications revenue stream. To further this initiative, AMA continues to add Supplemental Type Certificates ("STCs"), therefore broadening the aircraft types, models, and jurisdictions in which the afirs UpTime solution can be implemented. The process is a requirement that cannot be shortcut by any potential competitors and therefore, as the list of STCs grows, the barriers to entry increase.

As in previous years, customer installation schedules continue to be a challenge. Customer installation schedules are determined by "C Check" schedules. "C Checks" are the regular inspections made on all commercial aircraft after a set number of hours of operation of the aircraft or

a time limit, allowing for the installation of AMA's products. The Company obtains this schedule from a customer upon the signing of a contract, and manages the planned versus actual installations.

The acceptance of AMA as a global aviation solutions provider continues to be reinforced with the addition of agreements with industry heavyweights to the growing list of industry partners. During 2009 the Company added Sierra Nevada Corporation, GuestLogix Inc., and L-3 Communications Recorder Division to the distinguished list of partners such as Meggitt PLC. The Company continues to be involved and grow its presence in the global aviation industry through participation in various industry events and organizations. AMA's response to the Air France flight 447 mishap and its rapid delivery of FLYHTStream led to its involvement with various industry initiatives, the most notable being the European Oceanic Position Tracking Improvement and Monitoring ("OPTIMI") and the Critical Event Detection and Reporting ("CEDAR") as well as the roundtable talks organized by the French accident investigation branch, the Bureau d'Enquetes et d'Analyses pour la securite de l'aviation civile ("BEA"), into transoceanic tracking and data streaming.

Trends and Economic Factors

The Company continues to capitalize on the need for timely flight and sensor data from the aircraft to ground operations and maintenance facilities. Airlines are increasingly looking for methods to reduce costs and operate their aircraft more efficiently. Margins are extremely thin in the airline industry. Fuel and labour compete as the largest operating expenses for airlines, with fuel making up to approximately 25 percent of some airline's annual operating costs. The slightest decrease in fuel consumption can turn into big savings. Some of the fuel saving methods currently used by airlines include: using one engine instead of two while taxiing, tankering extra fuel, operating the Auxiliary Power Unit ("APU"), configuring the aircraft for most efficient flight profiles, and removing unnecessary equipment. These are examples of ways airlines can save fuel. The Company's afirs, UpTime, FIRST, and FLYHT Fuel Management System solutions are valuable tools that provide airlines with the data to save fuel costs and to improve operational efficiency and effectively manage aircraft operations. AMA customers are showing significant return on investment over the costs of afirs and UpTime.

In 2009 the Company continued to witness weakness across a variety of financial markets, resulting in continued volatility and uncertainty on a global basis together with recessionary conditions in many economies. The Company was not immune from the impact of these economic conditions. In particular, the aviation industry has been impacted by a slowdown in the demand for air travel, both business and vacation. The offset to the industry was continued moderated fuel costs from previous years, which continued to reduce operating costs and remove some of the pressure from the industry. The Company remains optimistic about its business outlook for 2010 as the global aviation industry moves out of the recessionary period that started in 2008 and continues to adopt technology that will help it monitor flight, operations, and maintenance issues to reduce costs. The Company has seen an upsurge in interest from legacy airlines for its technology as they strive to improve operational efficiency and reduce costs, and capital budgets return to pre-2008 levels. As well there has been a surge in interest from growing markets such as South America and the Middle East. Airlines in these markets have not seen the load factor declines of the legacy carriers and possess the capital budgets to improve the technology they are using to create efficient, low cost, technology driven operations.

The acquisition of the assets of a competitor, Wingspeed Corporation (“Wingspeed”), in October and the assumption of customer contracts and the restoration of service in December should increase monthly recurring revenue in 2010. The Company does not expect to see monthly recurring revenues at the same levels as existing AMA customers since the Wingspeed serviced customers contracted for a considerably lower level of deliverables. The Company does see the potential to sell value-added services to the Wingspeed customers as well as the opportunity to upgrade these customers to a full afirs UpTime solution over time.

The strengthening of the Canadian dollar relative to the US dollar during 2009 has negatively impacted the Company’s revenues and income. As a result of these movements, the Company’s Canadian dollar revenues, which are substantially all denominated in US dollars, were lower than would have been had the foreign exchange rates not changed. While a significant amount of the Company’s costs are denominated in Canadian dollars, a significant portion of marketing and parts costs are US Dollar denominated, and therefore create some natural hedge against the fluctuations of the Canadian dollar.

System Approvals

AMA has received STC approvals for afirs on the following aircraft:

- ✓ Airbus A319, A320, A321
- ✓ Airbus A330
- ✓ Boeing B737-200, 300, 400, 500
- ✓ Boeing B737-500, 600, 700, 800
- ✓ Boeing B757-200
- ✓ Boeing B767-200, 300
- ✓ Bombardier DHC-8-100, 200, 300
- ✓ Bombardier CRJ100, 200, 400
- ✓ Fokker F100
- ✓ Hawker Beech 750, 850XP, 900XP, 950XP
- ✓ DC-10
- ✓ Viking Air DHC-7 (LSTC)

AMA will be submitting STC approval for afirs in 2010 on the following aircraft:

- ✓ Airbus A300, A310
- ✓ Dessault Falcon
- ✓ Embraer Legacy

AMA has STC applications in process for afirs, expected to be submitted in 2010 on the following aircraft:

- ATR-42, 72
- Boeing 747-200,400
- MD-81/82/83/87/88

In addition, the company will be filing the necessary documents to obtain approval for the afirs 228 for all currently approved 220 STCs over the next several years.

Results of Operations – Year Ended December 31, 2009

Revenues

The following table shows afirs and UpTime revenue as well as other revenue, which consists of consulting services and interest revenue. The Company's long-term investment in marketing, research and development, and building relationships has resulted in a strong pipeline of prospective customers around the world. While 2009 has been a challenging year in the aviation industry, the Company believes that the ongoing revenue streams from our existing customer base will continue to expand throughout future years through the addition of services and fleet expansions. These efforts resulted in shipments totaling 44 during 2009 compared to 90 during 2008. AMA anticipates that shipment levels will return to historical levels as the aviation industry rebounds.

The Company has two types of revenue streams relating to afirs equipment depending on the type of service agreement: (1) leases and (2) sales. In accordance with the Company's revenue recognition policy for lease type agreements, the arrangement consideration is deferred as unearned revenue and revenue is recognized over the initial term of the contracts. In the early stages of the Company's growth this will result in less recognized revenue than cash received. For sales type agreements, afirs fees are deferred as unearned revenue and corresponding expenses are recorded as work in progress. When the system is fully functional and the customer has accepted the system, the deferred amount is fully recognized in revenue along with the work in progress as cost of sales. Under both forms of agreement, the UpTime usage fees are recognized as the service is provided based on actual customer usage that month. For the Sierra Nevada Corporation ("SNC") license fee, the amount received is deferred as unearned revenue and revenue is recognized over the initial 5 year term of the agreement. The amounts recorded in unearned revenue are non-refundable. The effect in the year is that AMA received \$7,471,777 (2008: - \$5,252,618) in cash revenue, which is calculated as \$5,106,494 (2008: - \$3,176,995) reported as financial statement revenue plus \$3,756,846 (2008: - \$2,186,541) being cash received for arrangement consideration less the portion of cash received during the year that is recognized in financial statement revenue of \$1,391,563 (2008 - \$110,918).

In 2009, revenue for the Company continued to reflect the benefits of the research and development efforts that have been invested over the past 9 years. AMA has products tested, certified, and installed on aircraft to generate revenue, as well as inventory to continue the rollout to our new and existing customers.

Total revenues were \$5,106,494 and \$3,176,995 for fiscal 2009 and 2008, respectively.

	2009			2008			2007		
	afirs UpTime	Other	Total	afirs UpTime	Other	Total	afirs UpTime	Other	Total
Q1	\$ 918,410	\$335,522	\$1,253,932	\$ 349,893	\$ 48,175	\$ 398,068	\$171,778	\$ 666,140	\$ 837,918
Q2	1,225,574	98,430	1,324,004	475,675	120,588	596,263	191,278	281,844	473,122
Q3	1,386,093	135,801	1,521,894	502,966	287,027	789,993	256,710	55,974	312,684
Q4	887,236	119,428	1,006,664	1,027,491	365,180	1,392,671	282,629	83,051	365,680
Total	\$4,417,313	\$689,181	\$5,106,494	\$2,356,025	\$820,970	\$3,176,995	\$902,395	\$1,087,009	\$1,989,404

Other revenue is derived from the sale of underfloor stowage units, the sale of consulting services, licensing fees, and interest. During 2009, underfloor stowage units revenue was \$228,465 (2008 – \$254,946), consulting revenue was \$196,454 (2008 - \$484,408), licensing fees were \$257,520 (2008 – \$Nil), and interest revenue was \$6,742 (2008 - \$81,616).

Gross Margin and Cost of Sales

Gross margin before general and administrative expenses was \$2,861,893 for 2009 (2008 - \$1,017,149). This increase was the result of the continued increase in afirs UpTime revenue and the move to sales type agreements from lease type agreements, which creates a better matching of revenue recognized to the cost of shipments and installation support.

Cost of sales for afirs, UpTime was \$2,092,831 on revenues of \$4,417,313 representing a gross margin of \$2,324,482 or 52.6% in 2009. This compares to 2008's \$1,978,679 cost of sales on revenues of \$2,356,025, representing a gross margin of \$377,346 or 16% on afirs UpTime revenue. The increase in the 2009 gross margin over 2008 on afirs UpTime is primarily due to an increased number of installed afirs units under the sales type agreements versus the lease type agreements, coupled with increased functionality. The revenue and expenses under the sales type agreements revenue recognition policy are aligned, which improves the margin versus lease type agreements where revenue is deferred and recognized over the term of the contract and expenses are recognized upon shipment.

Cost of sales on other revenue was \$151,770 on revenues of \$689,181, resulting in a gross margin of \$537,411 or 78.0%. In 2008 other revenue cost of sales was \$181,167 on revenues of \$820,970, resulting in a gross margin of \$639,803 or 77.9%. While there was a reduction in the overall gross margin for other revenue in 2009, it remained consistent on a percentage basis at 78%. The decrease in other revenue in 2009 is the result of a decrease in interest revenue and consulting services.

2009				
	Revenue	Cost of Sales	Gross Margin - \$	Gross Margin - %
afirs UpTime	\$ 4,417,313	\$ 2,092,831	\$ 2,324,482	52.6%
Other	689,181	151,770	537,411	78.0%
Total	\$ 5,106,494	\$ 2,244,601	\$ 2,861,893	56.0%

2008				
	Revenue	Cost of Sales	Gross Margin - \$	Gross Margin - %
afirs UpTime	\$ 2,356,025	\$ 1,978,679	\$ 377,346	16.0%
Other	820,970	181,167	639,803	77.9%
Total	\$ 3,176,995	\$ 2,159,846	\$ 1,017,149	32.0%

2007				
	Revenue	Cost of Sales	Gross Margin - \$	Gross Margin - %
afirs UpTime	\$ 902,395	\$ 1,206,506	\$ (304,111)	(33.7)%
Other	1,087,009	144,889	942,120	86.7%
Total	\$ 1,989,404	\$ 1,351,395	\$ 638,009	32.1%

Net Loss, General and Administrative and Marketing Expenses

In 2009, the key driver of our performance continued to be the timely closing of contracts with prospective customers, airline installation schedules of afirs on contracted aircraft due to their maintenance schedules, and the timely receipt of STC approvals from multiple regulators. The key challenge continues to be the speed with which potential customers execute contracts and the difficulty in predicting the accuracy of customer-supplied aircraft maintenance schedules. As well, the global downturn in the aviation industry adds the challenge of increasing the backlog of contracted aircraft. As a result, the net loss for the year ended December 31, 2009 was \$4,539,718 compared with \$8,523,228 loss for 2008. Efforts are being made to have OEMs install afirs in the factory and we hope to see movement in this regard in 2010.

Expense categories are not broken into departments for this year as the entire company was and is focused on getting our main products, afirs, UpTime, FLYHTStream, FIRST, and FLYHT Fuel Management System out to customers. For the year ended December 31, 2009, expenses were \$7,399,269 compared with \$9,540,377 for 2008.

Major Expense Categories	2009	2008	Variance	Explanation
Salaries and benefits, third party consulting, and share compensation	4,554,823	5,865,426	(1,310,603)	Staff levels in support positions decreased in 2009 causing salaries to decrease \$428,183 over 2009, and related statutory payments and benefits decreased \$45,992. To continue to attract and retain industry leading professionals, variable compensation was further instituted in 2009 resulting in increased variable compensation payments of \$96,000. The use of third party consultants was reduced in 2009 or the compensation arrangement was altered to be performance based resulting in a decrease in consulting costs of \$625,196. Share based compensation decreased by \$297,820 over 2009. Other staffing related expenses decreased \$10,223.
Research and development costs	574,444	745,308	(170,864)	The decrease in research and development is the result of decreased direct research and development activities during early 2009, but this trend reversed in the later half of the year with the commencement of research related to the new generation afirs hardware which will meet the requirements of regulatory changes in the aviation industry.
Office, computer services, insurance, depreciation stock exchange fees and bad debts	739,297	787,360	(48,063)	Office costs decreased \$48,063 primarily due to overall costs containment during 2008. The significant changes were a reduction in communication expenses of \$20,097 as the result of the introduction of an internet based phone system in late 2008. Bad debt expense decreased by \$134,244 due to increased diligence on collection of receivables and in 2008 one major customer declared bankruptcy which was not repeated in 2009. One time expenses related to the court appointment as interim manager of the Wingspeed assets for the period prior to the asset sale increased expenses by \$57,963. During 2009 expenses related to the relocation of the corporate offices and one recently hired industry leading professional was \$56,441. Foreign exchange loss increased \$27,222 from 2008 as the result of the strengthening of the Canadian dollar during 2009. Other office related expenses tracked either at the same level or lower than 2008.
Interest and bank charges	41,319	41,963	(644)	Bank charges decreased slightly in 2009.

Major Expense Categories	2009	2008	Variance	Explanation
Rent	400,784	240,589	160,195	Rent expense increased in 2009 as the result of the relocation of the corporate offices in early 2009. The increase was due to a combination of increased effective rental rate and the addition of office space to meet the needs of the Company.
Marketing	415,795	1,009,963	(594,168)	The decrease in marketing expenses is primarily related to the reduction in travel and associated travel expenses of \$546,966. This reduction was in response to the softening of the industry coupled with the use of various technologies to reduce the need to travel to potential customer locations. The Company expects the expenses in marketing to increase over the next year, as AMA continues to target global markets for its solutions and the industry rebounds to pre-2008 levels. Expenses related to marketing supplies and materials reduced \$47,202 from 2008 as there were adequate levels of inventory to meet the 2009 needs. Marketing costs do not include salaries.
Investor relations	85,656	158,330	(72,674)	Investor relations costs decreased \$72,674 due to the decreased emphasis on the use of investor show attendance and video presentations. The Company maintained a presence in the capital markets by presenting the Company to institutional investors, retail brokers, and retail investors via one on one meetings. The Company believes that one on one meetings are the most effective use of funds and anticipates that costs will increase in future years.
Professional fees	587,151	691,438	(104,287)	Legal fees were lower in 2009 by \$120,988 because of the withdrawal of the patent infringement action by a Toronto based company, which was partially offset by increased legal fees of \$22,400 relating to the filing of patent applications in 2009. Consulting fees were \$144,211 in 2009 compared to \$170,904 in 2008, a decrease of \$26,692. This decrease is primarily due to consulting related to the operations of Wingspeed of \$34,819 and a decrease of \$61,511 for third party consultants during 2009. Audit and accounting related expenses increased from \$78,270 in 2008 to \$121,664 in 2009 or \$43,394 due to increased audit expenses, IFRS consulting to prepare for the January 1, 2011 implementation, and the increased audit work associated with the purchase of the Wingspeed assets.
Total	7,399,269	9,540,377	(2,141,108)	

UpTime recurring fees should increase over time as more aircraft are installed with afirs and customers contract for the FIRST and FuelMI products that were introduced in 2009.

Quarterly Results

2009				
	Q4	Q3	Q2	Q1
Revenue	\$1,006,664	\$1,521,894	\$1,324,004	\$1,253,932
Loss	1,189,445	717,268	1,333,969	1,299,036
Loss/Share	0.01	0.01	0.02	0.02

2008				
	Q4	Q3	Q2	Q1
Revenue	1,392,671	789,994	596,263	398,067
Loss	1,912,469	1,814,010	2,709,237	2,087,512
Loss/Share	0.02	0.02	0.03	0.03

2007				
	Q4	Q3	Q2	Q1
Revenue	365,680	312,684	473,122	837,918
Loss	2,387,162	1,693,258	1,978,629	809,265
Loss/Share	0.04	0.03	0.03	0.01

UpTime recurring fees should increase over time as more aircraft are installed with afirs and customers contract for the FIRST and FuelMI products that were introduced in 2009.

Research and Development

Research and development (“R&D”) costs are being expensed as incurred. The majority of R&D costs are consulting expenses related to the design, testing, and manufacture of afirs, the design and testing of UpTime, and the design and testing of FIRST, FLYHTStream, and FLYHT Fuel Management System. During the last quarter of 2009, R & D commenced on the development of the next generation afirs known as afirs 228 (the “228”). This next generation product is aimed at meeting the global regulatory changes to air traffic control systems. The project budget for the 228 was approved by the Board of Directors at \$4.4 million through 2011. The Company anticipates receiving federal government funding to offset some of this R & D.

Foreign Exchange

All international sales of the Company’s products and services are denominated in U.S. dollars. Accordingly, the Company is susceptible to foreign exchange fluctuations. In 2009, over 98% of the Company’s gross sales were made in U.S. dollars compared to 97% in 2008. The Company expects this to continue since the aviation industry conducts a majority of its transactions in U.S. dollars, thus limiting the opportunity for sales in Canadian dollars or other major currencies. The Company will continue to look for opportunities to denominate agreements in other major currencies to reduce the exposure to fluctuations in the U.S. dollar.

Transactions with Related Parties

During the year, the Company’s transactions with a company owned by a director to supply consulting services and travel expenses totaled \$113,101 compared to \$73,694 in 2008. All of the transactions were at amounts that were agreed upon by the parties and approximated fair market value. The remaining transactions with related parties were normal business transactions related to their positions with the Company. These transactions were expense reimbursements for business travel and other company expenses paid by the related party and were measured at exchange amounts that the related party paid to a third party and were substantiated with a third party receipt.

Liquidity and Capital Resources

During 2009, the Company issued common shares through private and brokered placements and the exercise of stock options. This has improved the financial position of the Company, especially when coupled with the increased cash based revenue.

The Company issued 4,175,000 common shares on October 8th, 2009 pursuant to a non brokered private placement at \$0.40 resulting in gross proceeds of \$1,670,000. Pursuant to a brokered placement that closed on November 20th, 2009 the Company issued 16,000,000 units at \$0.50 for gross proceeds of \$8,000,000. Each unit consisted of one common share and one-half of one share purchase warrant where one full warrant is exercisable until May 20, 2011 at \$0.75. The net cash proceeds after issuance costs of the brokered placement totaled \$7,360,000. This brokered placement also included the issuing of an additional 1,120,000 agent warrants, which entitle the holder to acquire one common share at \$0.50 until November 20th, 2010. A further 823,167 common shares were issued to directors, officers, employees, and consultants on the exercise of stock

options. The weighted average issue price of these common shares was \$0.21, resulting in cash proceeds of \$173,467.

The successful equity offerings combined with increased cash based revenue throughout the year created sufficient capital to continue to operate and to provide capital for inventory to be deployed in order to expand our customer base.

Working capital at December 31, 2009 was \$7,572,447 compared to \$1,335,314 in 2008 an increase of \$6,237,133. The increase in working capital is primarily attributed to the net funds generated from the raising of capital equity of \$9,100,723 less the operating loss for the year of \$4,539,718; the remaining increase of \$1,675,735 is the result of various changes in working capital components as the result of business operations during the year.

Neither customer deposits nor the current portion of unearned revenue are refundable and if those two items were not included in the working capital calculation, the resulting modified working capital at December 31, 2009 would be \$9,785,744 compared to \$2,981,781 in 2008.

The Company currently has an available operating line of \$250,000 which had not been drawn at December 31, 2009. The operating line bears an interest rate of Canadian chartered bank prime plus 1.5% and is secured by assignment of cash collateral and a general security agreement.

The achievement of positive earnings before interest and amortization is necessary before the Company can improve liquidity. The Company has continued to expand its cash flow potential through its continued marketing drive to clients around the world. Management believes that the Company's installation momentum, conversion of installations to recurring revenue, new revenue streams, and ongoing sales will be sufficient to meet standard liquidity requirements. If general economic conditions or the financial condition of a major customer deteriorates then the Company may have to raise the necessary financing in the capital markets.

As at April 19, 2010, AMA's issued and outstanding shares was 103,582,386.

Contractual Obligations

The Company has entered into various leases for its operating premises and equipment. Future minimum annual payments under these operating leases are as follows:

Year	Premises	Equipment	Total
2010	419,619	119,165	538,784
2011	432,652	90,328	522,980
2012	445,685	32,319	478,004
2013	458,718		458,718
2014	76,815		76,815
	\$ 1,833,489	\$ 241,812	\$ 2,075,301

In addition, the Company has repayment obligations related to two Government of Canada loan programs. Under the Industrial Research Assistance Program (IRAP), the outstanding balance is \$246,134 (2008 – \$307,101), which is to be repaid, as a percentage of gross revenues, over a five to ten year period commencing in October 2005. Under the Technology Partnerships Canada (TPC) program, the Company has an outstanding balance of \$66,298 (2008 - \$85,410) to be repaid based on 15% of the initial contribution, which equates to \$19,122 per year for a 10 year repayment period. The yearly repayment is due if the Company has achieved more than a 10% increase in gross revenue over the previous year and the gross revenue exceeds the base gross revenue that was set in fiscal of 2004 of \$556,127. The repayment period commenced January 1st, 2005.

During 2009, AMA leased computer equipment totaling \$245,810 (2008 - \$47,350), which was accounted for as capital leases that expire in various years to 2012. The minimum lease payments are as follows:

Year	Total
2010	\$ 119,165
2011	90,328
2012	32,319
	\$ 241,812

The imputed interest is \$17,861 (2008 - \$17,575), leaving a total obligation of \$223,951 (2008 - \$55,425).

Results of Operations – Three Months Ended December 31, 2009

Revenues

During the fourth quarter \$725,565 (2008 - \$1,934,462) was received in cash revenue which is calculated as \$1,006,664 (2008 - \$1,392,672) and reported as financial statement revenue plus \$293,460 (2008 - \$624,805) being cash received for arrangement consideration less the portion of cash recognized during the quarter that is included in financial statement revenue of \$574,560 (2008 - \$83,015). Shipments during the fourth quarter totaled 7 compared to 25 during the same quarter of 2008.

Revenue decreased \$386,007 in the fourth quarter compared to the fourth quarter of last year, and afirs UpTime revenues decreased by \$95,032 over the fourth quarter of 2008. Product sales revenue decreased \$227,882 and services revenue and interest decreased \$63,093 over the same quarter of the previous year. The decrease in afirs UpTime revenue is the result of the decreased number of shipments during the quarter compared to the same quarter of 2008. This decrease can be directly attributed to the sluggishness of the aviation industry and the reduction in capital spending. The offset was an increase of 48.8% in recurring revenue in the quarter versus the same quarter of 2008 to \$579,248 from \$389,254, which indicates that the initiatives to maximize the revenue from installed equipment are bearing fruit. The decrease in product sales revenue can be directly attributed to a large volume of sales of underflow storage product in the fourth quarter of 2008 that did not occur in the same quarter of 2009. Product sales revenue historically fluctuates between quarters. The services revenue decrease was the result of consulting that was undertaken in the fourth quarter of 2008 for a major airline and an original equipment manufacturer as well as chargeable installation support for an airline customer. This type of consulting and installation support was not required in the fourth quarter of 2009.

Gross Margin and Cost of Sales

Cost of sales in the fourth quarter of 2009 is \$356,597 compared to \$847,179 in 2008, a decrease of \$490,582. The gross margin for the fourth quarter of 2009 was 64.6% versus 38.1% for the same period of 2008. Included in cost of sales are costs of non-routable parts and travel expenses for our engineers on initial installations of aircraft. Also, the introduction of the sales type agreement increased the gross margin as all cost of sales are recognized when the revenue is recognized instead of the revenue being recognized over the first term of the agreement and costs such as non-routable supplies and installation support being recognized when incurred. Accordingly, the change to sales type agreements has had the anticipated consequences with a cost of sales decline and an increase in margins. This is also coupled with increasing recurring revenue as a percentage of total revenue during the quarter, which will increase the overall margin as a percentage of sales since the cost of sales for recurring revenue is lower than that for afirs shipments and its corresponding non-routable supplies and support.

Net Loss, General and Administrative, and Marketing Expenses

The net loss for the quarter ended December 31, 2009 was \$1,189,445 (2008 - \$1,912,469). Included in general and administrative expenses are decreased marketing costs. Marketing expenses

decreased by \$97,356 to \$127,420 over the fourth quarter of 2008. The Company's focus is on generating new customers and as such will continue to engage resources in marketing; however, the sales and marketing team has focused on the use of technology to meet the needs of potential customers while minimizing the costs associated with marketing to the global aviation industry. The use of agents in key markets has further reduced the need for North American based sales personnel to travel as extensively. As the aviation industry rebounds and the demand for the Company's products and services increases there is an anticipation that marketing costs will increase.

Office expenses increased by \$29,566 in the fourth quarter over the same period of 2008, primarily due to a move of the corporate office in early 2009, increasing the fourth quarter rent expense by \$56,777 which was offset by a decrease in other general office expenses of \$27,211.

Salaries, the main cost of doing business, decreased to \$1,028,532 for the quarter versus \$1,504,493 for the fourth quarter of 2008, a \$475,961 decrease. This decrease is the result of the consolidation of functions and operational efficiencies that were instituted during 2009. The Company continues to hire qualified personnel as our customer base grows to ensure the Company is prepared for growth as the result of our strategic business alliances that continue to open opportunities. As these opportunities are solidified, it is expected that salaries will increase to meet the demands of the market place.

Stock-based compensation was \$81,737 in the fourth quarter of 2009 compared to \$34,757 in the same period of 2008. The increase was due to an option grant to non-executive employees in the quarter to recognize their service to the Company at a higher fair value than the corresponding option grant in the fourth quarter of 2008. As well, 50% of an option grant in May 2009 to a consultant vested during the quarter.

Research and Development

R & D costs are being expensed as incurred. The fourth quarter development costs for 2009 were \$133,392 as compared to \$258,158 in the same quarter of 2008. The decrease during the quarter was due to the timing of resources being placed into the planning process for the next generation afirs product in collaboration with Sierra Nevada Corporation as well as UpTime, FIRST, FLYHTStream, and FLYHT Fuel Management System. The majority of R&D costs are comprised of consulting expenses, testing and certification, and other expenses. Once the planning phase is completed in the early first quarter of 2010, the research and development costs will increase accordingly.

Critical Accounting Policies and Estimates

The Company prepares its consolidated financial statements in accordance with accounting principles generally accepted in Canada. The preparation of these financial statements requires Management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses. These estimates are based on management's historical experiences and various other assumptions that are believed by management to be reasonable under the circumstances. Such assumptions are evaluated on an ongoing basis and form the basis for making judgments about the

carrying value of assets and liabilities that are not readily apparent from other sources. Actual results could differ from these estimates.

The following are the Company's critical accounting policies, significant estimates, and assumptions used in preparing our financial statements:

1. The Company maintains an allowance for doubtful accounts for estimated losses that may occur if customers are unable to pay trade balances owing to the Company. This allowance is determined based on a review of specific customers, historical experience, and economic circumstances.
2. Inventories are carried at the lower of cost and net realizable value. Provisions for excess or obsolete inventory are recorded based on Management's assessment of the estimated market value of raw materials and afirs completed.
3. The Company evaluates its future tax assets and records a valuation allowance where the recovery of future taxes does not meet the required level of certainty. At December 31, 2009, valuation allowances are provided for the full amount of future tax assets.
4. The Company records amounts for warranty based on the actual costs associated with replacing components that are not functioning and these costs are recorded at the time a warranty claim is determined.
5. Intangible assets are stated at cost and comprise a license, customer contracts, and customer relationships. The license has an indefinite life. The customer contracts and relationships are amortized using the straight line method over the remaining life of the assumed contract. Intangible assets not subject to amortization are subject to an annual impairment test or more frequently if events or circumstances change that indicate that the carrying value may not be recoverable. Intangible assets subject to amortization are tested for impairment if events or circumstances indicate that the underlying value of the contract or relationship has changed.
6. The Company recognizes revenue from lease type agreements as agreement consideration, which is recorded as unearned revenue and recognized into revenue over the term of the lease agreement. Sales type agreement consideration is deferred as unearned revenue and corresponding expenses are recorded as work in progress until the system is fully functional and customer acceptance has been obtained at which time the full deferred amount is recognized in revenue along with the work in progress as cost of sales. For both types of agreements the revenue from UpTime usage fees is recognized at the end of each month and is based on actual usage during that month.

Underfloor stowage unit revenue is recognized when the unit is shipped and consulting services revenue is recognized when the services are completed.

Financial Instruments

The Company is exposed to fluctuations in the exchange rates between the Canadian dollar and other currencies with respect to assets, sales, and purchases. The Company monitors fluctuations and may take action if deemed necessary to mitigate its risk.

The Company is exposed to changes in interest rates as a result of the operating loan, bearing interest based on the Company's lenders' prime rate.

There is a credit risk associated with accounts receivable where the customer fails to pay invoices. The Company extends credit generally to credit-worthy or well-established customers. In the case of agreement consideration or product sales the invoiced amount is generally payable before the afirs or other product is shipped to the customer. The Company assesses the financial risk of a customer and based on that analysis will require that a deposit payment be made before a service is provided. As well, for monthly recurring revenue the Company has the ability to disable afirs UpTime and/or supply data in cases where the customer has not fulfilled its financial obligations.

Wingspeed Acquisition

On October 26, 2009, the Company purchased the assets of Wingspeed Corporation from the court-appointed receiver for cash consideration of \$310,780 and acquisition costs of \$194,220 for a total consideration of \$505,000. The purchase included but was not limited to the assumption of 3 customer contracts covering 51 aircraft, all intellectual property, tangible personal property, licenses and permits, product files, FAA Part 145 repair station status, and title and interest to know - how and technology. The operations of Wingspeed had ceased in August 2009, and AMA's primary goal after the acquisition was to restore service to the customers using onboard Wingspeed hardware and AMA's ground-based UpTime service. This was accomplished by the end of 2009, and recurring monthly service invoicing commenced in January 2010. The acquisition was accounted for under the new CICA Handbook Section 1581 "Business Combinations" and included in the financial results after October 26, 2009. Additional details relating to the acquisition are included in note 3 of the consolidated financial statements.

Contingencies

In September 2007, the Company, among others, was served with a counterclaim alleging that the Company induced a breach of contract and interfered with economic relationships. The Company maintains that the claims are without merit and no liability in respect to this action has been included in the consolidated financial statements, as management intends to vigorously defend the matter and believes the outcome will be in its favour. On November 7, 2007, the Company filed a statement of defense and a counterclaim against three parties for interference with legally binding contracts, disrupted business, attacks on the Company's reputation, and costs. Any amounts awarded as a result of these actions will be reflected in the year the amounts become reasonably estimable.

Adoption of New Accounting Standards

As of January 1, 2009, the Company adopted the newly issued accounting standard, CICA Handbook Section 3064 "Goodwill and Intangible Assets", relating to the method of accounting for goodwill and

intangible assets and the related disclosures. The adoption of these standards had no effect on the Company's consolidated financial statements.

Pending Pronouncements

The CICA issued Section 1582, "Business Combinations", which replaces former guidance on business combinations. Section 1582 establishes principles and requirements for the acquisition method for business combinations and related disclosures. This statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first reporting period beginning on or after January 2011 with earlier application permitted. The Company has chosen not to early adopt the new section.

The CICA issued Sections 1601, "Consolidated Financial Statements", and Section 1602, "Non-Controlling Interests", which replaces existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. The Company has chosen not to early adopt the new section.

International Financial Reporting Standards Changeover Plans

International Financial Reporting Standards ("IFRS") are to be implemented by the Company on January 1st, 2011 and CSA Notice 522-320 requires that progress on IFRS changeover plans be disclosed. AMA has completed a formal gap analysis of the differences between IFRS and Canadian GAAP. This analysis was reviewed by both the Audit Committee and external advisors. Based on that analysis the Company has commenced a detailed review and the preparation of white papers on areas of significant difference. To date AMA has identified the following areas where differences will occur but has not yet determined the potential impact on its financial statements. These areas are:

1. Property Plant & Equipment

The decision to adopt the cost model instead of revaluation will probably be made. Current depreciation rates have been reviewed and will most likely be deemed appropriate for all property, plant and equipment.

2. Impairment

IFRS results in increased exposure to impairment write downs. The movement from the existing afirs 220 to afirs 228 may result in impairment depending on the demand level for the afirs 220 at the time of transition. The Company has determined that it has a limited number of cost generating units ("CGU").

3. Leases

The Company has determined that there is no effect on the classification of capital versus operating leases.

4. IFRS 1

The most significant item under IFRS 1 will be determining the opening values for Property Plant and Equipment and if the cost model is appropriate. As well it is most likely that the election will be made to move cumulative translation gains and losses to Retained Earnings at December 31, 2009 as well as maintaining the investment value of FLYHT Inc. at the current carrying value.

The Company will continue to work in conjunction with its IFRS advisors to have the white papers and decisions made in the first half of 2010 with opening 2010 Balance Sheet completed and audited during the third quarter of 2010. The timing will be somewhat dependent on the availability of the IFRS consultant and AMA's auditors.

Management's Report

To the Shareholders of
AeroMechanical Services Ltd.

The accompanying consolidated financial statements of AeroMechanical Services Ltd. and all of the information in its annual report are the responsibility of Management and have been approved by the Board of Directors.

Management has prepared the consolidated financial statements in accordance with Canadian generally accepted accounting principles and where alternative accounting methods exist, Management has chosen those that it deems most appropriate.

Financial statements are not precise since they include amounts based on estimates and judgments. Such amounts have been determined on a reasonable basis to ensure the financial statements are presented fairly in all material aspects. Management has prepared the financial information in this annual report and has ensured it is consistent with the consolidated statements.

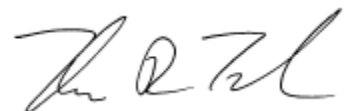
The AeroMechanical Board of Directors is responsible for ensuring Management fulfills its responsibilities for financial reporting and for reviewing and approving the financial statements. This is carried out principally through the Audit Committee. AMA's auditors have access to the audit committee.

The Audit Committee of the Board of Directors, consisting of a majority of independent members, meets regularly with management, as well as external auditors, to discuss auditing, internal controls, accounting policy, and financial reporting matters. The Committee reviews the financial statements with both management and the independent auditors and reports its findings to the Board of Directors before such statements are approved by the Board.



William Tempany
Chief Executive Officer

April 19, 2010



Thomas R. French, CGA
Chief Financial Officer

April 19, 2010

Auditors' Report

To the Shareholders of
AeroMechanical Services Ltd.

We have audited the consolidated balance sheets of AeroMechanical Services Ltd. as at December 31, 2009 and 2008 and the consolidated statements of loss and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants

Calgary, Canada

April 19, 2010

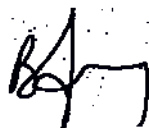
Consolidated Balance Sheets

December 31, 2009 and 2008

	2009	2008
Assets		
Current assets:		
Cash and cash equivalents	\$ 7,161,427	\$ 801,404
Restricted cash (note 10)	250,000	250,000
Accounts receivable	529,869	1,126,794
Deposits and prepaid expenses	288,177	349,005
Inventory (note 4)	2,418,375	1,787,811
	<u>10,647,848</u>	<u>4,315,014</u>
Property and equipment (note 5)	478,968	262,331
Rental assets (note 6)	143,539	1,347,508
Intangible assets (note 7)	478,403	34,992
	<u>\$ 11,748,758</u>	<u>\$ 5,959,845</u>
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 1,270,748	\$ 1,558,594
Current portion unearned revenue	1,589,313	1,289,466
Current portion of deferred leasehold inducements (note 8)	-	2,281
Current portion of loans payable (note 9)	109,536	105,068
Current portion of obligation under capital lease (note 11)	105,804	24,291
	<u>3,075,401</u>	<u>2,979,700</u>
Unearned revenue	1,534,529	812,608
Loans payable (note 9)	202,896	287,443
Obligation under capital lease (note 11)	118,147	31,134
	<u>4,930,973</u>	<u>4,110,885</u>
Shareholders' equity:		
Share capital (note 12)	35,550,028	28,982,059
Warrants (note 12)	4,181,685	1,717,678
Contributed surplus (note 12)	1,943,917	1,467,350
Deficit	(34,857,845)	(30,318,127)
	<u>6,817,785</u>	<u>1,848,960</u>
Going concern (note 1)		
Commitments (note 13)		
Contingencies (note 19)		
	<u>\$ 11,748,758</u>	<u>\$ 5,959,845</u>

See accompanying notes to the consolidated financial statements.

On behalf of the board



Director – William Tempany



Director – Paul Takalo

Consolidated Statements of Loss and Deficit

Years ended December 31, 2009 and 2008

	2009	2008
Revenue:		
afirs UpTime revenue	\$ 4,286,423	\$ 2,015,810
Product sales revenue	359,355	595,161
Services revenue and interest	460,716	566,024
	<u>5,106,494</u>	<u>3,176,995</u>
Cost of sales	<u>2,244,601</u>	<u>2,159,846</u>
Gross margin	2,861,893	1,017,149
Expenses:		
Salaries and benefits	4,147,003	5,160,967
General and administrative	1,542,365	1,502,596
Research and development	574,444	745,308
Stock based compensation	407,820	704,859
Marketing	415,795	1,009,963
Amortization	186,666	174,693
Foreign exchange loss	42,768	15,546
Interest and bank charges	41,319	41,563
Bad debts	41,089	175,334
Loss on asset disposal	-	9,548
	<u>7,399,269</u>	<u>9,540,377</u>
Net loss before income taxes	(4,537,376)	(8,523,228)
Current income taxes	2,342	-
Net loss and comprehensive loss	(4,539,718)	(8,523,228)
Deficit, beginning of year	(30,318,127)	(21,794,899)
Deficit, end of year	<u>\$(34,857,845)</u>	<u>\$(30,318,127)</u>
Net loss per share:		
Basic and diluted	\$ (0.05)	\$ (0.11)
Weighted average shares:		
Basic and diluted	<u>85,415,370</u>	<u>81,201,148</u>

See accompanying notes to the consolidated financial statements.

Consolidated Statements of Cash Flows

Years ended December 31, 2009 and 2008

	2009	2008
Cash provided by (used in):		
Operating activities:		
Net loss	\$ (4,539,718)	\$(8,523,228)
Add items not affecting cash		
Amortization	186,666	174,693
Amortization of rental assets	60,306	124,219
Amortization of intangibles	23,099	-
Stock based compensation	407,820	704,859
Loss on asset disposal	-	9,548
Write down of rental assets	83,289	75,117
Warranty expense	-	(13,842)
Unrealized foreign exchange loss	125,875	30,215
	<u>(3,652,663)</u>	<u>(7,418,419)</u>
Net change in non-cash working capital balances (note 18)	1,693,326	992,646
	<u>(1,959,337)</u>	<u>(6,425,773)</u>
Financing:		
Issuance of common shares	9,843,467	6,522,641
Repayment on capital leases	(75,262)	(33,756)
Share issue costs	(742,744)	(487,089)
Loan repayment	(80,079)	(42,978)
	<u>8,945,382</u>	<u>5,958,818</u>
Investments:		
Restricted cash	-	34,500
Purchase of property and equipment	(159,513)	(147,898)
Proceeds on disposal of property and equipment	-	1,500
Purchase of intangibles (note 3)	(466,509)	-
Purchase of rental assets	-	(565,430)
	<u>(626,022)</u>	<u>(677,328)</u>
Change in cash and cash equivalents	6,360,023	(1,144,283)
Cash and cash equivalents, beginning of year	801,404	1,945,687
Cash and cash equivalents, end of year	<u>\$ 7,161,427</u>	<u>\$ 801,404</u>

See accompanying notes to the consolidated financial statements.

Notes to Consolidated Financial Statements

Years ended December 31, 2009 and 2008

AeroMechanical Services Ltd. (the "Company") is a public company incorporated under the Canada Business Corporations Act. The Company is listed on the TSX Venture Exchange, trading under the symbol "AMA".

AMA is a designer, developer, and service provider to the global aerospace industry. The Company's major products are the Automated Flight Information Reporting System ("afirs™"), UpTime™, AeroQ™, FIRST, FLYHT Fuel Management System, FLYHTStream™, and underfloor stowage unit.

1. Going concern:

These consolidated financial statements have been prepared on the basis that the Company will continue to realize its assets and meet its obligations in the ordinary course of business. At December 31, 2009, the Company had working capital of \$7,572,447 (2008 – \$1,335,314), a deficit of \$34,857,845 (2008 - \$30,318,127), a net loss of \$4,539,718 (2008 - \$8,523,228), and negative cash flow from operations of \$2,403,805 (2008 - \$6,425,773).

The Company's ability to continue as a going concern is dependent upon attaining and sustaining profitable operations and/or obtaining additional financing in order to fund its on-going operations (note 17). The Company's ability to attain profitable operations and positive cash flow in the future is dependent upon various factors including its ability to acquire new customer contracts, the success of management's continued cost containment strategy, and general economic conditions.

There is no assurance that the Company will be successful in attaining and sustaining profitable operations and cash flows or raising additional capital to meet its working capital requirements. If the Company is unable to satisfy its working capital requirements from these sources, the Company's ability to continue as a going concern and to achieve its intended business objectives will be adversely affected. These financial statements do not reflect adjustments that would otherwise be necessary if the going concern assumption was not valid, such as revaluation to liquidation values and reclassification of balance sheet items.

2. Significant accounting policies:

The consolidated financial statements of the Company have been prepared in accordance with Canadian generally accepted accounting principles within the framework of the accounting policies as summarized below.

(a) Basis of presentation:

These financial statements consolidate the accounts of the Company and its wholly-owned subsidiaries, Flyht Inc, AeroMechanical Services USA Inc, Flyht Corp., and Flyht India Corp. The latter three subsidiaries were inactive for the reporting period and currently remain inactive. All inter-company transactions have been eliminated upon consolidation.

2. Significant accounting policies (continued):

(b) Use of estimates:

The preparation of the financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from and affect the results reported in these consolidated financial statements as future confirming events occur.

Amounts recorded for stock-based compensation are based on management's estimates of share price volatility and the expected life of the options. By their nature, these estimates are subject to uncertainty, and the impact on the consolidated financial statements of future periods could be material.

Amounts recorded for warranty are based on the actual costs associated with replacing components that are not functioning related to afirs UpTime.

Amounts recorded for provisions for obsolete inventory are based on management's estimates, which consider a variety of factors that may affect the carrying values of inventories. These factors include, but are not limited to, market demand, technology changes, and design changes.

(c) Revenue recognition:

The Company's main revenue sources are derived from the rental and sale of afirs units and related UpTime usage fees, and the sale of underfloor stowage units. There are two types of revenue streams: leases and sales, depending on the type of services agreement. Under the terms of lease type agreements, revenue from afirs is derived from an upfront fee which is recorded as unearned revenue and recognized into revenue over the term of the lease agreement. For sales type services agreements, afirs fees are deferred as unearned revenue and corresponding expenses are recorded as work in progress. When the system is fully functional and customer acceptance has been obtained, the full deferred amount is recognized in revenue along with the work in progress as cost of sales. Under both forms of agreement, revenue from UpTime usage fees is recognized at the end of each month and is based on actual usage during that month.

Revenue from the sale of underfloor stowage units is recognized when the unit is shipped, title is transferred, and collection is reasonably assured. Certain customers have prepaid for product services not yet delivered. These amounts are recorded as accounts payable and accrued liabilities on the balance sheet, and are recorded as revenue in the period in which such product or services are delivered.

2. Significant accounting policies (continued):

(d) Property and equipment:

Property and equipment is recorded at cost. Amortization is provided annually at rates calculated to write-off assets over their estimated useful lives as follows:

Computers	30% declining balance
Software	12 months straight-line
Equipment	20% declining balance
Leasehold improvements	Term of lease

(e) Rental assets:

Rental assets are recorded at cost and consist of afirs units that are leased and in use in customer aircraft. Amortization is provided for units that are leased on a straight line basis over 6 years.

(f) Future income taxes:

The Company uses the asset and liability method to account for income taxes. Future income taxes are calculated based on temporary differences arising between the financial statement carrying values and tax bases of assets and liabilities. Future income tax assets and liabilities are measured using substantively enacted income tax rates expected to apply in the years in which temporary differences are expected to be recovered or settled. Changes in income tax rates that are substantively enacted are reflected in the accumulated future tax balances in the period the change occurs. To the extent that future income taxes are not considered more likely than not to be realized, a valuation allowance is provided.

(g) Foreign currency translation:

Transactions denominated in US dollars have been translated into Canadian dollars at the approximate rate of exchange prevailing at the time of the transactions. Monetary assets and liabilities denominated in foreign currencies have been translated into Canadian dollars at the year end exchange rates.

The operations of the Company's foreign active subsidiary are considered self sustaining and therefore its accounts are translated into Canadian dollars under the current method of accounting whereby the assets and liabilities are translated into Canadian dollars using the exchange rate in effect at the consolidated balance sheet date. Revenues and expenses are translated at rates in effect at the time of the transactions. Exchange gains or losses on translation of the Company's net investment in the foreign operation are deferred in the cumulative adjustment component of shareholders' equity. Due to the timing and limited nature of the activities in the subsidiary in the current year, there were no exchange gains or losses on translation of the Company's net investment in the foreign operation. Other exchange gains and losses are included in the consolidated statement of loss and deficit.

2. Significant accounting policies (continued):

(h) Research and development costs:

Research costs are expensed as incurred. Development costs incurred in the design and development of new products are capitalized if certain defined criteria are met. The criterion for capitalization of development costs is met when the product is clearly identified, the technical feasibility has been established, management has indicated its intention to market the product, the future market is identified, and adequate resources exist or are expected to be available to complete the project. Upon commercial production or use of the product, deferred costs will be amortized over the estimated useful life of the product. If the criteria are no longer met, costs for a specific product are charged against earnings. To date, all development costs have been expensed as incurred.

(i) Financial instruments:

Financial instruments are initially classified into one of five categories: (i) held-for-trading, (ii) held-to-maturity, (iii) loans and receivables, (iv) available-for-sale, and (v) other financial liabilities. All financial instruments including all derivative instruments are recognized on the balance sheet initially at fair value. Subsequent measurement of all financial assets and liabilities – except those in the held-for-trading and available-for-sale categories – must be determined at amortized cost using the effective interest rate method. Held-for-trading financial instruments are measured at fair value with changes in fair value recognized in earnings. Available-for-sale financial instruments are measured at fair value with changes in fair value recognized in comprehensive income until the investment is derecognized or impaired, at which time the amounts would be recorded in net earnings.

The Company classifies its cash and cash equivalents and restricted cash as held-for-trading, accounts receivable are classified as loans and receivables. Accounts payable, certain accrued liabilities, and loans payable are classified as other liabilities, all of which are measured at amortized cost. Carrying values approximate the fair values due to the short term nature of the instruments.

(j) Inventory:

Raw material inventory is stated at the lower of cost and net realizable value. Management evaluates raw material inventory for obsolescence and charges obsolescence to cost of goods sold. Cost is determined using the first in first out method. Raw material inventories include underfloor stowage units and general parts which are held pending installation and sale to the customer.

afirs completed inventory is stated at the lower of cost and net realizable value. Cost is determined based on the cost of the raw material components plus a standard labour allocation. Management evaluates afirs completed inventory for obsolescence and charges obsolescence to cost of goods sold. afirs completed inventory consists of afirs units that have been assembled and are held pending sale to the customer.

2. Significant accounting policies (continued):

Installations in progress is stated at the lower of cost or net realizable value. Cost is determined based on the cost of the raw material components and direct installation project costs. Labour is not allocated to installation projects. Installations in progress consists of the direct costs associated with installation projects and is recognized when the system is fully functional and customer acceptance has been obtained, the installation in progress is recognized as cost of sales, and the full deferred revenue amount is recognized in revenue.

(k) Cash and cash equivalents:

Cash and cash equivalents consists of deposits in banks, redeemable deposits, Guaranteed Investment Certificates, and short-term investments with initial maturities of three months or less.

(l) Warranty:

Amounts recorded for warranty are based on the actual costs associated with replacing components that are not functioning and are recorded at the time a warranty claim is determined.

(m) Per share amounts:

The treasury stock method is used to determine the dilutive effect of stock options and other dilutive instruments. The treasury stock method assumes that proceeds received from the exercise of in-the-money instruments are used to repurchase common shares at the average market price for the period.

(n) Stock-based compensation:

The Company has a stock option plan for directors, officers, employees, and consultants of the Company. Under the terms of the stock option plan, the options shall be granted at an exercise price not less than market price of the stock on the date of issuance, less a discount up to a percentage permitted by the rules and policies of the stock exchange.

The Company records compensation expense in the consolidated statement of loss and deficit for stock options using the fair value method. Compensation costs are recognized over the vesting period, and are determined using the Black-Scholes option pricing model.

(o) Intangible assets:

Intangible assets are stated at cost and are comprised of a license and customer relationships. The license has an indefinite life. The customer relationships are amortized using the straight line method over the remaining life of the contract that was assumed on acquisition. Indefinite life intangible assets are subject to an annual impairment test or more frequent if events or changes in circumstances indicate that the carrying value may not be recoverable. Intangible assets subject to amortization are tested for impairment if events or circumstances indicate that the underlying value of the contract or relationship has changed.

2. Significant accounting policies (continued):

(q) Adoption of new accounting standards:

As of January 1, 2009, the Company adopted the newly issued accounting standard for goodwill and intangible assets, relating to the method of accounting for goodwill and intangible assets and the related disclosures. The adoption of these standards had no effect on the Company's consolidated financial statements.

(r) Pending Accounting Pronouncements

The CICA issued Section 1582, "Business Combinations", which replaces former guidance on business combinations. Section 1582 establishes principles and requirements for the acquisition method for business combinations and related disclosures. This statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first reporting period beginning on or after January 2011 with earlier application permitted. The Company has chosen not to early adopt the new section.

The CICA issued Sections 1601, "Consolidated Financial Statements", and Section 1602, "Non-Controlling Interests", which replaces existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. The Company has chosen not to early adopt the new section.

3. Business acquisition:

On October 26, 2009, the Company completed the acquisition of the assets of Wingspeed Corporation. The acquisition has been accounted for using the purchase method and is summarized as follows:

Inventory	\$	5,591
Property and equipment		32,900
Customer contracts		466,509
		<hr/>
	\$	505,000
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Consideration:		
Cash	\$	310,780
Acquisition costs		194,220
		<hr/>
Total Consideration	\$	505,000

4. Inventory:

	2009	2008
Raw material	\$ 1,139,816	\$ 1,374,771
afirs completed	561,268	-
Installations in progress	717,291	413,040
	\$ 2,418,375	\$ 1,787,811

5. Property and equipment:

2009	Cost	Accumulated amortization	Net book value
Computers	\$ 539,853	\$ 319,509	\$ 220,344
Software	228,120	158,073	70,047
Equipment	197,436	95,401	102,035
Leasehold improvements	103,850	17,308	86,542
	\$ 1,069,259	\$ 590,291	\$ 478,968

2008			
	Cost	Accumulated amortization	Net book value
Computers	\$ 420,211	\$ 261,702	\$ 158,509
Software	101,088	74,563	26,525
Equipment	144,658	72,065	72,593
Leasehold improvements	79,369	74,665	4,704
	\$ 745,326	\$ 482,995	\$ 262,331

Included in computers and equipment are capital leases with a cost of \$292,751 (2008 - \$98,418), accumulated amortization of \$114,185 (2008 - \$41,065) and a net book value of \$178,566 (2008 - \$57,352).

6. Rental assets:

2009	Cost	Accumulated amortization	Net book value
Rented assets	\$ 198,637	\$ 55,098	\$ 143,539
	\$ 198,637	\$ 55,098	\$ 143,539

2008			
	Cost	Accumulated amortization	Net book value
Rented assets	\$ 724,871	\$ 248,772	\$ 476,099
Assets available for sale or rental	1,089,926	218,517	871,409
	\$ 1,814,797	\$ 467,289	\$ 1,347,508

6. Rental assets (continued):

In 2009, it was determined that certain rental assets in the amount of \$83,289 (2008 – \$75,117) were obsolete. This obsolescence was recorded in cost of sales.

In 2009, the majority of services agreements were amended from rental type to sales type, which resulted in the transfer of assets available for sale or rental to inventory. The NBV of the assets transferred was \$588,906.

The remaining book value of rental assets as at December 31, 2009 relates to assets currently rented under 2 rental type agreements.

7. Intangible assets:

	Cost	Accumulated amortization	Net book value
2009			
License	\$ 34,992	\$ -	\$ 34,992
Customer relationships	466,510	23,099	443,411
	\$ 501,502	\$ 23,099	\$ 478,403
2008			
License	\$ 34,992	-	\$ 34,992
	\$ 34,992	\$ -	\$ 34,992

8. Deferred leasehold inducements:

	2009	2008
Balance, beginning of year	\$ 2,281	\$ 15,968
Amortization	(2,281)	(13,687)
Balance, end of year	-	2,281
Less: current portion	-	(2,281)
	\$ -	\$ -

9. Loans payable:

	2009	2008
<p>The Industrial Research Assistance Program "IRAP" loan is non-interest bearing and is repaid annually, based on 1.11% of gross revenues, commencing October 2005 and is unsecured. The current portion is calculated based on the actual gross revenues in the previous quarter plus the Company's revenue projections for the next nine months.</p>	\$ 246,134	\$ 307,101
<p>The Technology Partnerships Canada "TPC" loan is non-interest bearing and unsecured. The loan is repayable annually, based on 15% of the initial contribution when the Company has achieved more than 10% growth in gross revenues above the previous year's gross revenue and the gross revenue for the year is greater than the base amount. The base amount is defined as the Company's gross revenue in fiscal 2004, which was at \$556,127.</p>	66,298	85,410
	312,432	392,511
Less: current portion	(109,536)	(105,068)
	\$ 202,896	\$ 287,443

10. Bank loan:

The Company has available to it an operating demand loan up to a maximum of \$250,000 (2008 – \$250,000). The operating demand loan bears interest at Canadian chartered bank prime plus 1.5%. The operating demand loan and other revolving credit facilities are secured by an assignment of cash collateral in the amount of \$250,000 and a general security agreement including a first ranking security interest in all personal property. The amount of the cash collateral has been disclosed as restricted cash. As at December 31, 2009 and 2008, the facility had not been drawn.

11. Obligations under capital lease:

The Company is party to various capital leases for computer hardware and software that expire in 2012 or earlier. Future minimum lease payments under the capital leases are as follows:

	2009	2008
2009	\$ -	\$ 34,263
2010	119,165	22,107
2011	90,328	16,630
2012	32,319	-
	241,812	73,000
Less: imputed interest	(17,861)	(17,575)
Less: current portion	(105,804)	(24,291)
	\$ 118,147	\$ 31,134

12. Share capital:

(a) Authorized:

Unlimited numbers of:
Common shares
Classes A, B and C preferred shares, issuable in series

The preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares in each series and to determine the designation, rights, privileges, restrictions, and conditions attached to the shares in each series.

(b) Issued and outstanding:

	Number of shares	Value
Common shares:		
Balance December 31, 2007	72,720,622	\$ 23,992,644
Issued for cash	4,500,000	4,500,000
Bifurcation of warrants	-	(1,353,218)
Exercise of employee options	528,000	169,230
Contributed surplus from exercise of employee options	-	177,955
Exercise of warrants	4,751,597	1,853,411
Transfer from warrants on exercise	-	398,515
Share issue costs	-	(756,478)
Balance December 31, 2008	82,500,219	28,982,059
Issued for cash	20,175,000	9,670,000
Bifurcation of warrants	-	(2,240,000)
Exercise of employee options	823,167	173,468
Contributed surplus from exercise of employee options	-	101,485
Share issue costs	-	(1,136,984)
Balance December 31, 2009	103,498,386	\$ 35,550,028

12. Share capital (continued):

(c) Stock option plan:

The Company grants stock options to its directors, officers, employees and consultants. The Company has a policy of reserving up to 10% of the outstanding common shares for issuance to eligible participants. As at December 31, 2009, there were 10,349,839 (2008 – 8,250,022) common shares reserved for this purpose. All options vest immediately at the grant date with the exception of 75,000 (2008 – 33,333) options granted to a consultant during 2009 which have not yet vested. The options are granted at an exercise price not less than fair market value of the stock on the date of issuance. A summary of the Company's outstanding and exercisable stock options, as at December 31, 2009 and 2008 and changes during these years is presented below:

	2009		2008	
	Number of shares	Weighted average exercise price	Number of shares	Weighted average exercise price
Outstanding, beginning of year	2,308,998	\$ 0.52	2,235,668	\$ 0.50
Granted	1,955,000	0.31	1,752,000	0.54
Exercised	(823,167)	0.21	(528,000)	0.32
Cancelled/expired	(656,335)	0.69	(1,150,670)	0.57
Outstanding, end of year	2,784,496	\$ 0.42	2,308,998	\$ 0.52
Exercisable, end of year	2,709,496	\$ 0.43	2,275,665	\$ 0.52

Weighted average life remaining for the options outstanding and exercisable is 2.7 years.

The weighted average fair market value of the options granted during the year was \$0.31 (2008 - \$0.54) per option. The fair value of the options granted was estimated using the Black-Scholes option pricing model with the following weighted average assumptions:

	2009	2008
Risk-free interest rate	1.34%	2.73%
Expected life (years)	2.5	2.4
Volatility in the price of the Company's common shares	124%	163%
Dividend yield rate	0.00%	0.00%

12. Share capital (continued):

(d) Contributed surplus:

	2009	2008
Balance, beginning of year	\$ 1,467,350	940,445
Employee stock options exercised	(101,486)	(177,955)
Agent options expired	170,233	-
Stock based compensation	407,820	704,859
Balance, end of year	\$ 1,943,917	\$ 1,467,350

(e) Warrants:

A summary of the Company's outstanding warrants and changes during the years are presented below:

	2009	2008
Balance, beginning of year	\$ 1,717,678	\$ 493,589
Finder fee warrants exercised	-	(398,515)
Warrants issued on private placement	2,240,000	1,353,218
Agent options issued	394,240	269,387
Agent options expired	(170,233)	-
Balance, end of year	\$ 4,181,685	\$ 1,717,678

	2009		2008	
	Number of warrants	Weighted average exercise price	Number of warrants	Weighted average exercise price
Outstanding, beginning of year	2,572,500	\$ 1.31	9,535,960	\$ 0.52
Granted	9,119,999	0.72	2,722,500	1.27
Exercised	-	-	(4,751,597)	0.44
Expired	(315,000)	1.00	(4,934,363)	0.75
Outstanding, end of year	11,377,499	\$ 0.84	2,572,500	\$ 1.31

On October 8, 2009 the Company issued 4,175,000 common shares at \$0.40 per share in connection with a non brokered private placement for net cash proceeds of \$1,670,000.

On November 20, 2009 the Company issued 16,000,000 units at \$0.50 per unit in connection with a brokered private placement with each unit consisting of one common share and one-half of one purchase warrant for net cash proceeds of \$7,360,000.

12. Share capital (continued):

In connection with this brokered private placement 7,999,999 warrants were issued entitling the holder to acquire one common share of the Company at \$0.75 until May 20, 2011.

The estimated fair value of these warrants is \$2,240,000 or \$0.28 per warrant. The fair value of these warrants was estimated using the Black-Scholes option pricing model with average risk-free interest rate of 1.14%, expected life of 1.5 years, volatility in the price of the Company's common shares of 133% and dividend yield of 0.00%.

The remaining 1,120,000 warrants were issued in connection with the brokered private placement completed on November 20, 2009, and consisted of agent warrants entitling the holder to acquire one common share of the Company at \$0.50 until November 20, 2011. These agent warrants are accounted for as a charge to share issuance costs of \$394,240 or \$0.35 per warrant. The fair value of the agent warrants were estimated using the Black-Scholes option pricing model with a weighted average risk-free interest rate of 1.14%, expected life of 2.0 years, volatility in the price of the Company's common shares of 128%, and a dividend yield rate of 0.00%.

13. Commitments:

The Company is party to various leases for its operating premises and equipment. Future minimum annual payments under these operating leases are as follows:

2010	\$ 538,784
2011	522,980
2012	478,004
2013	458,718
2014	76,815
	\$ 2,075,301

14. Related party transactions:

During the year, the Company contracted with a company owned by a director to supply consulting services and travel expenses totaling \$113,101 (2008 - \$73,694). All of the transactions were measured at the exchange amounts, that being the amount of consideration established and agreed upon by the related parties and approximated fair market value.

15. Income taxes:

(a) The income tax expense differs from the amounts which would be obtained by applying the expected Federal and provincial income tax rate of 29.00% (2008 – 29.5%) as follows:

	2009	2008
Computed "expected" tax (recovery)	\$ (1,321,798)	\$ (2,514,352)
Non-deductible expenses	11,303	22,512
Stock-based compensation	118,268	207,933
Rate change and other	352,873	363,322
Valuation allowance and other	841,696	1,920,585
	\$ 2,342	\$ –

(b) The components of the Company's future income tax assets are as follows:

	2009	2008
Capital assets	\$ 30,304	\$ 19,652
Intangibles	17,607	(857)
Inventory	7,706	-
Non-capital loss carry-forwards	7,084,002	6,239,744
Share issue costs	278,104	215,546
Scientific research and experimental development expenditures	1,125,987	1,138,337
Other	56,212	14,643
Valuation allowance	(8,599,922)	(7,627,065)
	\$ –	\$ –

(c) The Company has non-capital losses for income tax purposes of approximately \$28,222,949 which are available to be applied against future year's taxable income. The benefit of these non-capital losses has not been recognized in the consolidated financial statements. These losses will expire as follows:

2010	1,715,370
2014	2,570,288
2015	2,461,959
2026	3,390,309
2027	5,596,948
2028	8,293,252
2029	4,194,823
	\$ 28,222,949

16. Financial instruments and financial risk management:

The carrying values of cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities approximate their fair value due to the relatively short periods to maturity of these instruments. The fair value of the loans payable could not be determined as the timing of repayment is difficult to estimate since they are dependant on future revenues.

The nature of these instruments and the Company's operations expose the Company to the following risks:

(a) Credit risk:

Credit risk reflects that the Company may be unable to collect amounts due to the Company from customers for its services, products, or other transactions that may be entered into by the Company. The extent of risk depends on the credit quality of the party from which the amount is due.

The Company employs established credit approval and monitoring practices to mitigate this risk, including evaluating the creditworthiness of new customers and monitoring customer payment performance. The Company also includes the ability to receive payments in advance for both services and products in its agreements with customers as well as the ability to suspend services and ongoing support. The Company establishes an allowance for doubtful accounts that corresponds to the credit risk of its customers, historical trends, and economic circumstances.

The aging of the accounts receivable as at year end is as follows:

	2009
Current, 1 – 30 days	\$ 428,012
31 – 60 days	53,672
61 – 90 days	1,264
Greater than 90 days	46,921
	\$ 529,869

The movement in the allowance for doubtful accounts as at year end is as follows:

	Provision
Balance, December 31, 2008	\$ -
Provision	41,089
Accounts receivable written off	(682)
Balance, December 31, 2009	\$ 40,407

16. Financial instruments and financial risk management (continued):

(b) Interest risk:

The Company is exposed to interest rate risk on cash balances earning interest income and to the extent that it may draw on its operating line of credit which calculates interest as a function of variable interest rates. As at December 31, 2009, the Company does not carry material liabilities that are exposed to variable interest rates.

(c) Liquidity risk:

The Company is exposed to liquidity risk to the extent it is unable to collect its trade receivable balances on a timely basis and generate additional services revenue, which in turn could impact the Company's ability to meet commitments to creditors. The Company manages its liquidity risks by carrying cash on its balance sheet, by maintaining a conservative capital structure, by prudently managing its credit risks, and by maintaining its relationship with the capital markets to meet any near-term liquidity requirements.

(d) Foreign exchange risk:

The Company is exposed to foreign exchange risk primarily in the following ways:

- (i) Cash flow – a significant portion of the Company's revenues and a portion of its expenses are denominated in US dollars. Management estimates that a 1% weakening of the Canadian dollar would increase net earnings by approximately \$48,512 (2008 - \$30,342) and a strengthening of the Canadian dollar would decrease net earnings by approximately \$48,512 (2008 - \$30,342).
- (ii) Working capital – the Company has exposure to foreign exchange risk for working capital items denominated in US dollars. At December 31, 2009, working capital denominated in US dollars was approximately \$139,928 (2008 - \$760,506). As a result a 1% weakening of the Canadian dollar would increase net earnings by approximately \$1,399 (2008 - \$7,606) and a strengthening of the Canadian dollar would decrease net earnings by approximately \$1,399 (2008 - \$7,606).

The Company mitigates its exposure to foreign exchange risk in the following ways:

- (iii) Cash flow – the Company mitigates its cash flow exposures by the international nature of the business where a significant portion of its marketing costs are in currencies that naturally hedge a portion of US dollar revenue. The Company has not engaged in activities to manage its cash flow foreign currency exposure through the use of financial instruments.
- (iv) Working capital – the Company mitigates its working capital exposure by managing its US dollar denominated working capital items to limit the requirement to convert either to or from US dollars to fulfill working capital payment requirements.

17. Capital management:

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern (note 1) so that it can continue to seek to provide returns for shareholders and benefits for other stakeholders, to maintain optimal structure to reduce the cost of capital, and to facilitate the growth strategy of the Company.

The Company monitors its capital management through analysis of cash flow expectations to ensure an adequate amount of liquidity and through the monthly review of financial results and business expectations. The Company considers the shareholders' equity to be the capital of the Company.

Based upon the dynamic nature of the aviation and technology markets that the Company engages in, and the low level of tangible assets required, the capital strategy is to carry a low level of debt, including capital leases. Although a formal debt to equity ratio has not been established by the Company, the ratio of debt to equity at December 31, 2009 was 7.9% (2008 – 24.2%)

18. Supplemental cash flow information:

Change in non-cash working capital:

	2009	2008
Changes in non-cash working capital:		
Accounts receivable	\$ 471,050	\$ (535,283)
Deposits and prepaid expenses	60,827	919
Inventory	429,810	22,672
Accounts payable and accrued liabilities	(287,848)	338,617
Unearned revenue	1,021,768	1,179,408
Deferred lease inducement	(2,281)	(13,687)
	\$ 1,693,326	\$ 992,646
Interest (paid)/earned	\$ (11,139)	\$ 67,378

Cash and cash equivalents:

	2009	2008
Cash in bank	\$ 7,161,427	\$ 386,404
Guaranteed investment certificates	-	415,000
	\$ 7,161,427	\$ 801,404

19. Contingency:

In September 2007, the Company, among others, were served with a counterclaim alleging that the Company induced a breach of contract and interfered with economic relationships. The Company maintains that the claims are without merit. Management intends to vigorously defend the matter and believes the outcome will be in its favour. On November 7, 2007, the Company filed a statement of defense and a counterclaim against three parties for interference with legally binding contracts, disrupted business, attacks on the Company's reputation, and costs. Any amounts awarded as a result of these actions will be reflected in the year the amounts become reasonably estimable.

Corporate Information

Directors

Bill Tempany	CEO of the Company
Richard Hayden	President of the Company
Doug Marlin	President of Marlin Ventures Ltd.
Mike Brown	Partner, Geselbracht Brown
Paul Takalo, CA	Vice-President, Standen's Limited
Jack Olcott	President, General Aviation Company

Officers

Bill Tempany	CEO
Richard Hayden	President
Thomas French, CGA	CFO
Matt Bradley	VP Business Development

Auditor

KPMG LLP	Calgary, Alberta
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Legal Counsel

Chris Croteau	Tingle Merrett LLP
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Offices

Head Office	200W, 1144 - 29 Avenue NE Calgary, Alberta T2E 7P1
US Office	Suite 130-310, 2951 Marina Bay Drive League City, TX 77573



AeroMechanical Services Ltd.

200W, 1144 – 29 Avenue NE

Calgary, AB, Canada T2E 7P1

Phone: 403-250-9956

Fax: 403-291-9717

www.amscanada.com