


AeroMechanical Services Ltd.

2007 Annual Report
Financials

TSX.V: AMA





Managements' 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 Company maintains internal accounting and administrative controls designed to provide reasonable assurance that the financial information is relevant, reliable, and accurate and that the Company's assets are appropriately accounted for and adequately safeguarded.

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. AeroMechanical'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.

Signed ("William Tempany")

Chief Executive Officer
Calgary, Alberta
April 9, 2008

Signed ("Thomas R. French")

Chief Financial Officer
Calgary, Alberta
April 9, 2008



Auditors' Report

To the Shareholders of

AeroMechanical Services Ltd.

We have audited the consolidated balance sheet of AeroMechanical Services Ltd. as at December 31, 2007 and the consolidated statements of loss and deficit and cash flows for the year 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 audit.

We conducted our audit 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, 2007 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The consolidated statements as at December 31, 2006 and for the year then ended were audited by other auditors, who expressed an opinion without reservation on those statements in their report dated April 9, 2007.

KPMG LLP

Chartered Accountants

Calgary, Alberta

April 9, 2008

Consolidated Balance Sheets As at December 31,

	2007	2006
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 1,945,687	\$ 2,688,389
Restricted cash – Note 7	284,500	284,500
Accounts receivable	621,726	291,603
Prepaid expenses	349,924	233,040
Inventory	1,810,483	428,886
	5,012,320	3,926,418
Property and equipment – Note 3	252,826	224,644
Rental assets – Note 4	981,414	768,696
Intangible assets	34,992	34,992
	\$ 6,281,552	\$ 4,954,750
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	\$ 1,219,977	\$ 497,531
Current portion unearned revenue	232,805	101,774
Current portion of deferred leasehold inducements – Note 5	13,687	13,687
Current portion of loans payable – Note 6	52,810	120,742
Current portion of obligation under capital lease – Note 8	23,681	16,105
	1,542,960	749,839
Unearned revenue	689,861	292,920
Deferred leasehold inducements – Note 5	2,281	15,968
Loans payable – Note 6	382,679	351,959
Obligation under capital lease – Note 8	18,150	27,028
Warranty	13,842	12,016
	2,649,773	1,449,730
SHAREHOLDERS' EQUITY		
Share capital – Note 9	23,992,644	17,052,282
Contributed surplus – Note 9	1,434,034	1,379,323
Deficit	(21,794,899)	(14,926,585)
	3,631,779	3,505,020
	\$ 6,281,552	\$ 4,954,750

Going concern – Note 1, Commitments – Note 10, Subsequent event – Note 15, Contingencies – Note 16
See accompanying notes to the consolidated financial statements

On behalf of the board

Signed (“William Tempany”)
Director

Signed (“Douglas Marlin”)
Director

Consolidated Statements of Loss and Deficit Years Ended December 31,

	2007	2006
REVENUE		
Rental revenue	\$ 709,191	\$ 607,864
Sales revenue	386,363	290,810
License fees and interest	893,850	195,792
	1,989,404	1,094,466
Cost of sales	1,351,395	861,147
Gross margin	638,009	233,319
EXPENSES		
Salaries and benefits	4,098,886	2,226,301
General and administrative	1,400,126	1,104,486
Marketing	1,079,353	618,508
Stock based compensation	525,252	455,985
Research and development	253,236	248,902
Amortization	89,038	62,170
Foreign exchange loss	36,338	22,795
Interest and bank charges	24,094	33,878
	7,506,323	4,773,023
Net loss and comprehensive loss	\$ (6,868,314)	\$ (4,539,706)
Deficit, beginning of year	\$ (14,926,585)	\$ (10,386,879)
Deficit, end of year	\$ (21,794,899)	\$ (14,926,585)
NET LOSS PER SHARE		
Basic and diluted – Note 2 (n)	\$ (0.11)	\$ (0.10)

See accompanying notes to the consolidated financial statements

Consolidated Statements of Cash Flows Years Ended December 31,

	2007	2006
CASH PROVIDED BY (USED IN):		
OPERATING ACTIVITIES		
Net loss	\$ (6,868,314)	\$ (4,539,706)
Add items not affecting cash		
Amortization	89,038	62,170
Amortization of rental assets	82,749	53,198
Stock based compensation	525,252	455,985
Write down of rental assets	122,400	-
Warranty expense	1,825	(224)
Unrealized foreign exchange loss (gain)	26,232	(5,237)
	(6,020,818)	(3,973,814)
Net change in non-cash working capital balances – Note 14	(591,873)	(869,922)
	(6,612,691)	(4,843,736)
FINANCING		
Issuance of common shares	6,583,616	8,845,723
Repayment on capital leases	(18,444)	(4,521)
Share issue costs	(122,884)	(786,462)
Loan repayment	(37,213)	(13,310)
	6,405,075	8,041,430
INVESTMENTS		
Restricted cash	-	(284,500)
Purchase of property and equipment	(117,220)	(121,229)
Purchase of intangible assets	-	(34,992)
Purchase of rental assets	(417,866)	(152,593)
	(535,086)	(593,314)
Change in cash and cash equivalents	(742,702)	2,604,380
Cash and cash equivalents, beginning of year	2,688,389	84,009
Cash and cash equivalents, end of year	\$ 1,945,687	\$ 2,688,389

See accompanying notes to the consolidated financial statements



Notes to Consolidated Financial Statements Years Ended December 31, 2007 and 2006

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

The Company is a designer, developer and service provider to the global aerospace industry. The major products are the Automated Flight Information Reporting System ("afirs™"), UpTime™, AeroQ™ and Underfloor Stowage Units.

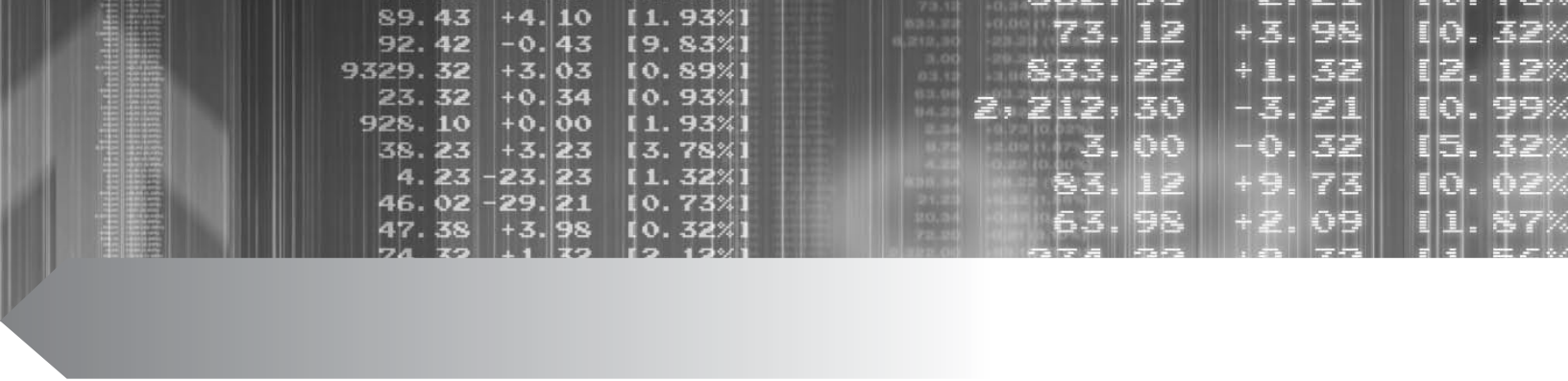
NOTE 1 GOING CONCERN

At December 31, 2007, the Company had working capital of \$3,469,360 (2006 – \$3,176,579), a deficit of \$21,794,899 (2006 – \$14,926,585), a loss from operations of \$6,868,314 (2006 – \$4,539,706) and negative cash flow from operations of \$6,612,692 (2006 – \$4,843,736).

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 15). 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 containments 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 could be adversely affected.

These consolidated financial statements have been prepared on the basis that the Company will continue to meet its obligations in the ordinary course of business and 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.



NOTE 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 subsidiary, AeroMechanical Services USA Inc, Flyht Corp. and Flyht India Corp. These subsidiaries were inactive for the reporting period and currently remain inactive.

(b) Measurement Uncertainty

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 management's estimates of the costs associated with the afirs™ rental assets. Costs of technology up-grades and replacing components that are not functioning plus associated costs of travel and staff time have been included in the estimates. 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 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 of afirs™ units and related UpTime™ usage fees and the sale of under floor storage boxes. Revenue from afirs™ is derived from an upfront fee which is recorded as unearned revenue and recognized into revenue over the term of the 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 under floor storage boxes 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 unearned revenue on the balance sheet and are recorded as revenue in the period in which such product or services are delivered.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES Continued

(d) Property and Equipment

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

Computers	30% declining balance
Equipment	20% declining balance
Leasehold improvements	60 months straight-line

(e) Rental Assets

Rental assets are recorded at cost and consist of afirs™ units that are in use in customer aircraft, spare units held by airlines and units available for lease. Amortization is provided for those units that are leased on a straight line basis over 6 years.

(f) Future Income Taxes

The Company uses the 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. A valuation amount is recorded against any future income tax assets that substantially consists of non-capital loss carry forwards, if it is more likely than not the asset will not be realized.

(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 subsidiary are considered integrated and therefore its accounts are translated into Canadian dollars under the temporal method of accounting whereby monetary items are translated at exchange rates in effect at the balance sheet date and non-monetary items translated at rates of exchange in effect when assets were acquired or obligations incurred. Revenues and expenses are translated at rates in effect at the time of the transactions. Exchange gains and losses are included in the consolidated statement of loss and deficit.

(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 criteria 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.

89.43	+4.10	[1.93%]	73.12	+3.98	10.32%
92.42	-0.43	[9.83%]	833.22	+1.32	12.12%
9329.32	+3.03	[0.89%]	2,212.30	-3.21	10.99%
23.32	+0.34	[0.93%]	3.00	-0.32	15.32%
928.10	+0.00	[1.93%]	83.12	+9.73	10.02%
38.23	+3.23	[3.78%]	63.98	+2.09	11.87%
4.23	-23.23	[1.32%]			
46.02	-29.21	[0.73%]			
47.38	+3.98	[0.32%]			
74.32	+1.32	[2.12%]			

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES Continued

(i) Financial Instruments

The Company adopted as of January 1, 2007 the new standards issued by the Canadian Institute of Chartered Accountants ("CICA") regarding the recognition, measurement, disclosure and presentation of financial instruments. Under these standards, financial instruments must be 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. The new standards require that all financial instruments within the scope of the standards, including all derivative instruments be 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 adoption of these new standards had no impact on the Company's accounts and deficit position as at December 31, 2007. As a result of the adoption of these new standards, the Company has classified its cash and cash equivalents as held-for-trading, accounts receivable are classified as loans and receivables. Accounts payable and certain accrued liabilities 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. The fair value of the loans payable could not be determined as the timing of the repayment are difficult to estimate as they are dependent on future revenues.

(j) Comprehensive Income

The Company also adopted as of January 1, 2007 new standards with respect to comprehensive income. The new standards require a statement of comprehensive income, if there are items that give rise to comprehensive income or loss. The Company did not identify any such items giving rise to comprehensive income or loss in the year ended December 31, 2007, or that would result in an adjustment to opening balances for accumulated other comprehensive income or loss.

(k) Inventory

Inventory is stated at the lower of cost and net realizable value. Management evaluates inventory for obsolescence and charges obsolescence to cost of goods sold. Cost is determined using the first in first out method. Inventories include under floor storage units and general parts which are held pending installation and sale to the customer.

(l) 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.

(m) Warranty

Provisions for estimated expenses related to product warranties are made at the time products are leased. These estimates are established using historical information relating to the nature, frequency, and average cost of warranty claims.

NOTE 2 SIGNIFICANT ACCOUNTING POLICIES Continued

(n) 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.

The weighted average number of shares outstanding during the year was 64,304,464 (2006 – 45,085,226).

(o) Stock-based Compensation

The Company has an executive stock compensation plan and a stock option plan for directors, officers, employees and consultants of the Company. The executive stock compensation plan provides for direct grants of stock to the Company's officers. 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 are determined using the Black-Scholes option pricing model.

(p) Intangible Assets

Intangible assets are stated at cost and are comprised of a license. The license has an 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.

(q) Deferred Leasehold Inducements

Leasehold inducements are deferred and amortized against rent expense on a straight-line basis over the term of the lease. When a lease interest is abandoned, the balance of the leasehold inducement is offset against the lease buyout cost or rent expense during the applicable period.

(r) New Accounting Standards Effective January 1, 2008

The Company will adopt new accounting standards relating to inventory and disclosure and presentation of financial instruments. Management does not anticipate that these new standards will have a material impact on the Company's financial statements.

(s) Comparative Figures

Certain of the comparative figures have been reclassified to conform to the presentation adopted in the current year.

NOTE 3 PROPERTY AND EQUIPMENT

2007	Cost	Accumulated Depreciation	Net Book Value
Computer	\$ 331,950	\$ 197,578	\$ 134,372
Equipment	153,376	57,469	95,907
Leasehold improvements	79,369	56,822	22,547
	\$ 564,695	\$ 311,869	\$ 252,826

2006	Cost	Accumulated Depreciation	Net Book Value
Computer	\$ 256,072	\$ 153,136	\$ 102,936
Equipment	113,714	40,351	73,363
Leasehold improvements	77,689	29,344	48,345
	\$ 447,475	\$ 222,831	\$ 224,644

Included in computer and equipment are capital leases with a net book value of \$39,627 (2006 – \$38,213).

NOTE 4 RENTAL ASSETS

2007	Cost	Accumulated Depreciation	Net Book Value
Leased assets	\$ 705,942	\$ 172,246	\$ 533,696
Assets available for lease	591,118	143,400	447,718
	\$ 1,297,060	\$ 315,646	\$ 981,414

2006	Cost	Accumulated Depreciation	Net Book Value
Leased assets	\$ 400,560	\$ 89,497	\$ 311,063
Assets available for lease	479,233	21,600	457,633
	\$ 879,793	\$ 111,097	\$ 768,696

In 2007, it was determined that certain rental assets in the amount of \$122,400 (2006 – nil) were obsolete. These rental assets have been charged against income on the consolidated statements of loss and deficit.

NOTE 5 DEFERRED LEASEHOLD INDUCEMENTS

	2007	2006
Balance, beginning of year	\$ 29,655	\$ -
Additions		37,640
Amortization	(13,687)	(7,985)
Balance, end of year	15,968	29,655
Less: current portion	(13,687)	(13,687)
	\$ 2,281	\$ 15,968

NOTE 6 LOANS PAYABLE

	2007	2006
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.	\$ 330,966	\$ 349,066
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.	104,523	123,635
	\$ 435,489	\$ 472,701
Less: current portion	(52,810)	(120,742)
	\$ 382,679	\$ 351,959

NOTE 7 BANK LOAN

Operating demand loan is available to the Company up to a maximum of \$250,000 (2006 – \$250,000). The operating demand bears interest at Canadian chartered bank prime plus 1.0%. The operating demand loan and other revolving credit facilities are secured by an assignment of cash collateral in the amount of \$284,500 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, 2007, the facility has not been drawn.

NOTE 8 OBLIGATIONS UNDER CAPITAL LEASE

The Company is party to various capital leases for computer hardware and software that expire in 2009. Future minimum lease payments under the capital leases are as follows:

	2007	2006
2008	\$ 29,400	\$ 23,202
2009	16,275	21,801
2010	4,003	8,780
	49,678	53,873
Less: imputed interest	(7,847)	(10,650)
Less: current portion	(23,681)	(16,105)
	<u>\$ 18,150</u>	<u>\$ 27,028</u>

NOTE 9 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, 2005	\$ 27,849,007	\$ 7,975,377
Issued for cash	24,868,959	8,751,430
Issued on settlement of debt	5,450,227	1,672,793
Exercise of employee options	320,630	103,383
Contributed surplus from exercise of employee options	-	18,347
Share subscription receivable	-	(9,090)
Share issue costs	-	(1,459,958)
Balance December 31, 2006	58,488,823	17,052,282
Issued for cash	6,519,467	2,929,180
Exercise of employee options	1,259,993	430,966
Contributed surplus from exercise of employee options	-	290,632
Exercise of warrants	6,452,339	3,223,470
Contributed surplus from exercise of warrants	-	179,908
Share subscription receivable	-	9,090
Share issue costs	-	(122,884)
Balance December 31, 2007	<u>\$ 72,720,622</u>	<u>\$ 23,992,644</u>

NOTE 9 SHARE CAPITAL Continued

(b) Issued and Outstanding (continued)

- (i) In 2006, the Company issued 8,543,959 units at \$0.26 per unit for cash proceeds of \$2,221,430 and net cash proceeds, net of all issuance costs, of \$1,993,437. Each unit consists of one common share and one-half of one purchase warrant. One whole warrant may be exercised into one common share at a price of \$0.40 and the warrants expire on February 9, 2008. The warrants are subject to an acceleration clause whereby if the Company's common share price is equal to or greater than \$0.50 for a period of 10 consecutive trading days, the Company may notify all warrant holders and issue a press release causing the warrants to be exercised within 30 days of the date of the press release, failing which the warrants expire.
- (ii) In 2006, the Company issued 16,250,000 units at \$0.40 per unit for cash proceeds of \$6,500,000 and net cash proceeds, net of all issuance costs, of \$5,942,031. Each unit consists of one common share and one-half of one purchase warrant. One whole warrant may be exercised into one common share at a price of \$0.60 if exercised on or before September 1, 2007 and at a price of \$0.75 if exercised prior to September 1, 2008.

(c) Stock Option Plan

The Company grants stock options to its directors, officers 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, 2007, there were 7,272,062 (2006 – 5,848,882) common shares reserved for this purpose. All options vest immediately at the grant date with the exception of 150,000 performance options granted to employees during the year. 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 option grants, as at December 31, 2007 and December 31, 2006 and changes during the years are presented below:

	2007		2006	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of year	2,426,995	\$ 0.33	1,333,720	\$ 0.42
Granted	1,139,000	0.65	1,580,000	0.28
Exercised	(1,259,993)	0.34	(320,630)	0.29
Cancelled/expired	(70,334)	\$ 0.57	(166,095)	\$ 0.55
Outstanding, end of year	2,235,668	\$ 0.50	2,426,995	\$ 0.33
Exercisable, end of year	2,119,002	\$ 0.48	2,426,995	\$ 0.33

Of the options outstanding 116,666 are not vested or exercisable at December 31, 2007 since performance conditions had not yet been met.

NOTE 9 SHARE CAPITAL Continued

Range of Exercise Price	Number Outstanding	Options Outstanding	
		Weighted Average Contractual Life (years)	Weighted Average Exercise Price
\$0.21 to \$0.70	2,235,668	2.2	\$ 0.50

Range of Exercise Price	Number Outstanding	Options Exercisable	
		Weighted Average Contractual Life (years)	Weighted Average Exercise Price
\$0.21 to \$0.70	2,119,002	2.2	\$ 0.50

The weighted average fair market value of the options granted during the year was \$0.65 (2006 – \$0.28) per option. The fair value of the options granted was estimated using the Black-Scholes option pricing model with the following weighted average assumptions:

	2007	2006
Risk-free interest rate	4.6%	3.9%
Expected life (years)	2.6	2.9
Volatility in the price of the Company's common shares	190%	197%
Dividend yield rate	0.00%	0.00%

(d) Contributed Surplus

	2007	2006
Balance, beginning of year	\$ 1,379,322	\$ 268,187
Finder fee warrants exercised	(179,908)	673,497
Employee stock options exercised	(290,632)	(18,347)
Stock based compensation	525,252	455,985
Balance, end of year	\$ 1,434,034	\$ 1,379,322

NOTE 9 SHARE CAPITAL Continued

(e) Warrants

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

	2007		2006	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding, beginning of year	17,136,376	\$ 0.51	3,046,497	\$ 0.45
Finder fee granted	-	-	780,681	0.26
Granted	-	-	4,271,982	0.40
Granted	-	-	8,125,000	0.60
Finder fee granted	-	-	1,304,396	0.60
Exercised	(6,452,339)	0.49	(75,000)	0.40
Expired	(1,148,077)	0.45	(317,140)	0.65
Outstanding, end of year	9,535,960	\$ 0.52	17,136,376	\$ 0.51

The 14,482,059 warrants issued in 2006 entitle the holder to acquire one common share of the Company at prices ranging from \$0.40 to \$0.75. Of the issued warrants 9,429,396 were issued with escalating exercise price of \$0.60 until September 1, 2007 and \$0.75 until September 1, 2008. Of the remaining warrants, 2,521,500 warrants expire February 9, 2008, 2,531,163 warrants expire March 7, 2008, the 9,429,396 expire on September 1, 2008.

The fair value of these warrants were \$3,951,389 or \$0.32 per warrant. The fair value of these warrants were estimated using the Black-Scholes option pricing model with average risk-free interest rate of 3.9%, expected life of 1.7 years, volatility in the price of the Company's common shares of 202% and dividend yield of 0.00%. The fair value attributed to the warrants has not been bifurcated from the value of the units issued. As such, the full value of the units issued has been allocated to share capital.

Finder fee warrants are accounted for as a charge to share issuance costs and a credit to contributed surplus (Note 9 (e)). The fair value of the finder fee warrants were estimated using the Black-Scholes option pricing model with a weighted average risk-free interest rate of 3.9%, expected life of 1.7 years, volatility in the price of the Company's common shares of 202%, and a dividend yield rate of 0.00%.

NOTE 10 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:

2008	\$ 240,205
2009	68,481
2010	13,896
2011	11,580
	\$ 334,162

89.43 +4.10 [1.93%]
 92.42 -0.43 [9.83%]
 9329.32 +3.03 [0.89%]
 23.32 +0.34 [0.93%]
 928.10 +0.00 [1.93%]
 38.23 +3.23 [3.78%]
 4.23 -23.23 [1.32%]
 46.02 -29.21 [0.73%]
 47.38 +3.98 [0.32%]
 74.32 +1.32 [2.12%]

73.19 +0.34 [0.46%]
 833.22 +1.32 [0.16%]
 2,212.30 -3.21 [0.15%]
 3.00 -0.32 [10.67%]
 83.12 +9.73 [11.59%]
 63.98 +2.09 [3.27%]
 93.32 +0.32 [0.34%]

NOTE 11 RELATED PARTY TRANSACTIONS

During the year, the Company had normal course business transactions with related parties, all of which were measured at the exchange amounts, that being the amount of consideration established and agreed upon by the related parties and approximates fair market value.

During 2006 the Company had the following transactions with related parties, all of which were measured at the exchange amounts, that being the amount of consideration established and agreed upon by the related parties and approximates fair market value.

- (a) The Company issued 3,532,899 common shares to officers and directors of the Company at \$0.30 per share in settlement of debt of \$1,059,870.
- (b) The Company issued 617,500 units to officers and directors of the Company at \$0.26 per unit for cash proceeds of \$160,550. Each unit consists of one common share and one-half of one purchase warrant. Each whole warrant may be exercised into one common share at a price of \$0.40 and the warrants expire on February 9, 2008. The warrants are subject to an acceleration clause whereby if the Company's common share price is equal to or greater than \$0.50 for a period of 10 consecutive trading days, the Company may notify all warrant holders and issue a press release causing the warrants to be exercised within 30 days of the date of the press release, failing which the warrants expire.

NOTE 12 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 32.12% (2006 – 32.49%) as follows:

	2007	2006
Computed "expected" tax (recovery)	\$ (2,206,102)	\$ (1,474,950)
Non-deductible expenses	20,676	11,397
Stock-based compensation	168,711	148,150
Rate change and other	823,123	645,403
Valuation allowance and other	1,193,592	670,000
	<u>\$ -</u>	<u>\$ -</u>

NOTE 12 INCOME TAXES Continued

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

	2007	2006
Capital assets	\$ 148,108	\$ 92,012
Intangibles	51	56
Warranty liability	3,607	3,485
Non-capital loss carry-forwards	4,709,586	3,874,612
Share issue costs	192,018	255,857
Scientific research and experimental development expenditures	648,953	283,437
Other	4,161	(2,316)
Valuation allowance	(5,706,484)	(4,507,143)
	<u>\$ -</u>	<u>\$ -</u>

(c) The Company has non-capital losses for income tax purposes of approximately \$18,072,288 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:

2008	211,463
2009	561,577
2010	1,715,370
2014	2,570,288
2015	2,419,758
2026	4,258,514
2027	6,335,318
	<u>\$ 18,072,288</u>

NOTE 13 FINANCIAL INSTRUMENTS

(a) Foreign Currency Risk

The Company is exposed to fluctuations in the exchange rates between the Canadian dollar, and other currencies with respect to assets, sales and purchase. The fluctuations are expensed as incurred. The Company monitors fluctuations and takes action, if deemed necessary, to mitigate its risks.

(b) Credit Risk

Accounts receivable include amounts receivable for normal terms and extended terms, which are generally made to credit worthy purchasers. The Company is exposed to losses in the event of non-performance by counter-parties to these financial instruments.

NOTE 14 SUPPLEMENTAL CASH FLOW INFORMATION

	2007	2006
Change in Non-Cash Working Capital		
Accounts receivable	\$ (330,123)	\$ (76,731)
Prepaid expenses	(116,884)	(180,732)
Inventory	(1,381,597)	(145,001)
Accounts payable and accrued liabilities	722,446	(611,693)
Unearned revenue	527,972	144,235
Deferred lease inducement	(13,687)	-
	\$ (591,873)	\$ (869,922)
Taxes paid	-	-
Interest earned	\$ 85,132	\$ 4,798
Cash and Cash Equivalents		
Cash in bank	\$ 430,187	\$ 122,889
Guaranteed investment certificates	1,515,500	2,565,500
	\$ 1,945,687	\$ 2,688,389

NOTE 15 SUBSEQUENT EVENT

On March 13, 2008, the Company issued 4,500,000 units at \$1.00 per unit for net proceeds of \$4,041,460. Each unit consists of one common share and one-half purchase warrant. Each whole warrant may be exercised any time into one common share at a price of \$1.30 and expire March 12, 2010.

Since December 31, 2007 the Company issued 4,476,597 common shares on the exercise of warrants for cash proceeds of \$ 1,767,411 and 481,000 common shares on the exercise of stock options for cash proceeds of \$135,360.

NOTE 16 CONTINGENCIES

The Company is defending itself in two actions instigated by the same plaintiff and the Company believes that, as the amount of liability is undetermined at this time, no liability has been accrued for claims on these actions:

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 and no liability in respect to this action has been included in these 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.

In September 2007, the Company was served with a claim of patent infringement seeking unspecified damages. The Company maintains that the claims are without merit and no liability in respect to this action has been included in these consolidated financial statements as management intends to vigorously defend the matter and believes the outcome will be in its favour. On December 24, 2007 the Company filed a Motion to Dismiss which was heard on April 8, 2008 and dismissed with the caveat that the plaintiff could file an amended complaint by April 30, 2008 in which both inventors are named as parties. 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
Darryl Jacobs	President of the Company, Co-Founder
Doug Marlin	President of Marlin Ventures Ltd.
Mike Brown	Partner, Geselbracht Brown
Christine Larkin	Senior Manager, BDO Dunwoody LLP
Tim Morgan	President, Morgan Air.

Officers

Bill Tempany	CEO
Darryl Jacobs	President
Johannes Brom	COO
Tom French	CFO
Pat Sandall	VP Sales & Marketing

Auditor

KPMG LLP	Calgary, Alberta
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Legal Counsel

Chris Croteau	Tingle Merrett LLP
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Offices

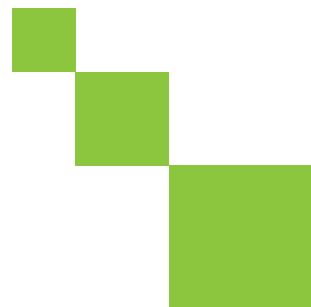
Head Office	#300, 2421 - 37 Avenue NE Calgary, Alberta T2E 6Y7
US Office	Suite 130-310, 2951 Marina Bay Drive League City, TX 77573

Members of Audit Committee

Bill Tempany	CEO of the Company
Doug Marlin	President of Marlin Ventures Ltd.
Christine Larkin	Senior Manager, BDO Dunwoody LLP

Members of Compensation Committee

Doug Marlin	President of Marlin Ventures Ltd.
Mike Brown	Partner, Geselbracht Brown
Tim Morgan	President, Morgan Air.



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AeroMechanical Services Ltd.

300, 2421 - 37 Ave NE
Calgary, AB Canada T2E 6Y7

Phone: 1-403-250-9956
Toll-free: 1-866-250-9956
Facsimile: 1-403-291-9717
Email: investors@amscanada.com

238.27	-7.93	[8.12%]
928.10	+3.03	[0.89%]
38.23	+0.34	[0.93%]
4.23	+0.00	[1.93%]
46.02	-3.23	[1.32%]
47.38	+3.98	[0.32%]
74.32	-3.21	[0.99%]
2,494.87	-0.32	[5.32%]
2.48	+9.73	[0.02%]
332.45	+2.09	[1.87%]
86.39	+3.03	[0.89%]
4.21	+0.34	[0.93%]
132.09	+0.00	[1.93%]
33.83	+2.23	[3.78%]
57.92	-2.23	[1.32%]
23.33	-2.21	[0.73%]
832.98	+3.98	[0.32%]
73.12	0.00	[2.12%]
833.22	0.00	[0.99%]
8,212.30	0.00	[5.32%]
3.00	+9.73	[0.02%]
83.12	+2.09	[1.87%]
63.98	+9.73	[0.02%]
234.22	+0.34	[0.93%]
2.32	-0.21	[0.73%]
24.13	+3.33	[0.33%]
74.75	+0.32	[2.22%]
89.43	+4.10	[1.93%]
92.42	-0.43	[9.83%]
9329.32	+3.03	[0.89%]
23.32	+0.34	[0.93%]
928.10	+0.00	[1.93%]
38.23	+3.23	[3.78%]

