

AeroMechanical Services Ltd.

2009 Financial Statements

TSX.V: AMA



AeroMechanical Services Ltd.



Management's Report

To the Shareholders of
AeroMechanical Services Ltd.

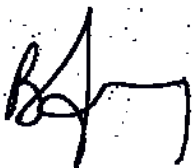
The accompanying consolidated financial statements of AeroMechanical Services Ltd. and all of the information in its annual report are the responsibility of Management and have been approved by the Board of Directors.

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.

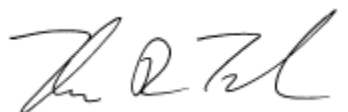
Financial statements are not precise since they include amounts based on estimates and judgments. Such amounts have been determined on a reasonable basis to ensure the financial statements are presented fairly in all material aspects. Management has prepared the financial information in this annual report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



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 Tempamy



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	<u>(30,318,127)</u>	<u>(21,794,899)</u>
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
	<u>\$ 505,000</u>
Consideration:	
Cash	\$ 310,780
Acquisition costs	194,220
Total Consideration	<u>\$ 505,000</u>

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			
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			
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
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.	\$ 246,134	\$ 307,101
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.	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

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