AIR INDUSTRIES GROUP, INC

CONSOLIDATED FINANCIAL STATEMENTS and FOOTNOTES

DECEMBER 31, 2009 and 2008

Air Industries Group, Inc.

Index to Consolidated Financial Statements and Footnotes

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REPORT OF INDEPENDENT REGISTERED ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Air Industries Group, Inc.

We have audited the accompanying consolidated balance sheets of Air Industries Group, Inc. and Subsidiaries (the "Company") as of December 31, 2009 and 2008 and the related consolidated statements of operations, changes in stockholders' equity and cash flows for the years then ended. The consolidated 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 the standards of the Public Company Accounting Oversight Board (United States). These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2009 and 2008 and the results of their operations and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 1, the Company restated its 2008 consolidated financial statements to reflect corrections for the reclassification of expenses totaling $286,000 from accounts payable and accrued expenses to cost of goods sold, and the reclassification of expenses totaling $45,000 from property and equipment to cost of goods sold. As a result of the restatement, net loss attributable to common stockholders for the year ended December 31, 2008 increased by $331,000 ($1.88 per share). Stockholders' equity decreased by a like amount.

Rotenberg Meril Solomon Bertiger & Guttilla, P.C.

Rotenberg Meril Solomon Bertiger & Guttilla, P.C.
Saddle Brook, New Jersey
December 21, 2010

AIR INDUSTRIES GROUP, INC.
Consolidated Balance Sheets at December 31,

		2009		2008
ASSETS				
Current Assets				
Cash and Cash Equivalents	$	165,000	$	164,000
Accounts Receivable, Net of Allowance for Doubtful Accounts of $161,000 and $302,000		5,575,000		5,279,000
Inventory		21,568,000		21,099,000
Assets Held for Sale		248,000		1,556,000
Prepaid Expenses and Other Current Assets		267,000		147,000
Taxes Receivable		49,000		53,000
Deposits - Customers		94,000		100,000
Total Current Assets		27,966,000		28,398,000
Property and Equipment, net		4,933,000		5,462,000
Capitalized Engineering Costs – net of Accumulated Amortization of $1,418,000 and $562,000		1,688,000		2,033,000
Deferred Financing Costs, net, deposit and other assets		656,000		994,000
Intangible Assets, net		1,943,000		2,126,000
Goodwill		291,000		291,000
TOTAL ASSETS	$	37,477,000	$	39,304,000
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities				
Current Portion Notes Payable and Capitalized Lease Obligations	$	20,711,000	$	16,904,000
Accounts Payable and Accrued Expenses		6,034,000		5,453,000
Lease Impairment - Current		223,000		-
Deferred Gain on Sale - Current Portion		38,000		38,000
Dividends Payable		460,000		366,000
Liabilities Held for Sale		2,093,000		2,878,000
Total Current Liabilities		29,559,000		25,639,000
Long term liabilities				
Notes Payable and Capitalized Lease Obligation - Net of Current Portion		3,104,000		5,973,000
Lease Impairment - Net of Current Portion		356,000		-
Deferred Tax Liability		-		1,364,000
Deferred Gain on Sale - Net of Current Portion		599,000		637,000
Deferred Rent		610,000		420,000
TOTAL LIABILITIES		34,228,000		34,033,000
Commitments and contingencies				
STOCKHOLDERS' EQUITY				
Preferred Stock Par Value $.001-Authorized 8,003,716 shares Designated as Series "A" Convertible Preferred - $.001 par Value, 1,000 Shares Authorized 0 Shares issued and outstanding as of December 31, 2009 and December 31, 2008, respectively.		-		-
Designated as Series "B" Convertible Preferred -$.001 Par Value, 4,000,000 shares authorized, 2,627,714 and 1,387,205 shares issued and outstanding as of December 31, 2009 and December 31, 2008, respectively; Liquidation Value, $ 26,277,000		3,000		1,000
Common Stock - $.001 Par, 120,000,000 Shares Authorized, 179,245 and 178,811 Shares Issued and Outstanding as of December 31, 2009 and 2008, respectively		-		-
Additional Paid-In Capital		24,063,000		23,029,000
Accumulated Deficit		(20,817,000)		(17,759,000)
Total Stockholders' Equity		3,249,000		5,271,000
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	37,477,000	$	39,304,000

See notes to consolidated financial statements

AIR INDUSTRIES GROUP, INC.
Consolidated Statement of Operations for the Years Ended December 31,

	2009	2008
Net Sales	$ 44,851,000	$ 38,694,000
Cost of Sales	36,703,000	29,964,000
Gross Profit	8,148,000	8,730,000
Operating Expenses	6,453,000	10,018,000
Impairment of Lease	579,000	-
Impairment of Goodwill	-	4,532,000
Total Operating Expenses	7,032,000	14,550,000
Income (loss) from operations	1,116,000	(5,820,000)
Interest and financing costs	(5,448,000)	(2,780,000)
Other (Loss) Income	(1,000)	58,000
Loss before benefit from income taxes	(4,333,000)	(8,542,000)
Benefit from income taxes	(1,699,000)	(744,000)
Loss From Continuing Operations	(2,634,000)	(7,798,000)
Loss From Discontinued Operations	(424,000)	(9,076,000)
Net Loss	(3,058,000)	(16,874,000)
Dividend attributable to preferred stockholders	1,431,000	620,000
Net loss attributable to common stockholders	$ (4,489,000)	$ (17,494,000)
Loss per share (basic and diluted)		
Continuing Operations	$ (25.07)	$ (47.90)
Discontinued Operations	-	(51.65)
Total	$ (25.07)	$ (99.55)
Weighted average shares outstanding (basic and diluted)	179,054	175,730

See notes to consolidated financial statements

AIR INDUSTRIES GROUP, INC.
Consolidated Statement of Stockholders Equity For the Years Ended December 31, 2008 and 2009

	Series A Preferred Stock		Series B Preferred Stock		Common Stock		Additional Paid-in	Accumulated	Total Stockholders'
	Shares	Amount	Shares	Amount	Shares	Amount	Capital	Deficit	Equity
Balance, January 1, 2008	-	$ -	829,098	$ 1,000	69,122,189	$ 69,000	$ 18,744,000	$ (885,000)	$ 17,929,000
Reverse Stock Split	-	-	-	-	(68,949,384)	(69,000)	69,000	-	-
Issuance of Stock to Employees under stock incentive plan	-	-	-	-	350	-	34,000	-	34,000
Non-cash dividends for Series B Preferred Stock	-	-	98,758	-	-	-	-	-	-
Dividend on Series B Preferred Stock - 2008	-	-	-	-	-	-	(246,000)	-	(246,000)
Dividend on Series B Preferred Stock - 2007	-	-	-	-	-	-	146,000	-	146,000
Issuance of Stock as part of June 2008 financing transaction	-	-	-	-	2,458	-	195,000	-	195,000
Issuance of Stock as part of June 2008 financing transaction	-	-	236,000	-	-	-	1,584,000	-	1,584,000
Issuance of Stock for fee relating to June 2008 financing transaction	-	-	-	-	500	-	40,000	-	40,000
Stock issued for services rendered	-	-	-	-	688	-	52,000	-	52,000
Conversion of Preferred Stock to Common Stock	-	-	(23,091)	-	2,010	-	1,000	-	1,000
Issuance of Stock to investors related to September 2008 financing transaction	-	-	156,400	-	-	-	1,048,000	-	1,048,000
Issuance of Stock for fee relating to September 2008 financing transaction	-	-	39,640	-	-	-	265,000	-	265,000
Issuance of Stock to investors related to October 2008 financing transaction	-	-	50,400	-	-	-	338,000	-	338,000
Issuance of Warrants related to financing transactions	-	-	-	-	-	-	556,000	-	556,000
Stock compensation expense	-	-	-	-	-	-	203,000	-	203,000
Net loss	-	-	-	-	-	-	-	(16,874,000)	(16,874,000)
Balance, December 31, 2008	-	-	1,387,205	$ 1,000	178,811	$ -	$ 23,029,000	$ (17,759,000)	$ 5,271,000
Non-cash dividends for Series B Preferred Stock	-	-	1,127,838	2,000	-	-		-	2,000
Dividend on Series B Preferred Stock - 2009	-	-	-	-	-	-	(460,000)	-	(460,000)
Dividend on Series B Preferred Stock - 2008	-	-	-	-	-	-	246,000	-	246,000
Issuance of Stock to investors related to January 2009 financing transaction	-	-	35,600	-	-	-	261,000	-	261,000
Issuance of Stock for fee relating to January 2009 financing transaction	-	-	3,560	-	-	-	-	-	-
Issuance of Stock in exchange for sellers' notes payable	-	-	58,500	-	-	-	640,000	-	640,000
Issuance of Stock to vendor in settlement of outstanding balance	-	-	5,011	-	-	-	25,000	-	25,000
Issuance of Stock in Settlement of HSM-Blair transaction	-	-	10,000	-	-	-	100,000	-	100,000
Issuance of Stock to vendor in settlement of outstanding balance	-	-	-	-	434	-	-	-	-
Reversal of dividends payable of Series A Preferred Stock	-	-	-	-	-	-	120,000	-	120,000
Stock compensation expense	-	-	-	-	-	-	102,000	-	102,000
Net loss	-	-	-	-	-	-	-	(3,058,000)	(3,058,000)
Balance, December 31, 2009	**-**	**$ -**	**2,627,714**	**$ 3,000**	**179,245**	**$ -**	**$ 24,063,000**	**$ (20,817,000)**	**$ 3,249,000**

See notes to consolidated financial statements

AIR INDUSTRIES GROUP, INC.
Consolidated Statement of Cash Flows For the Year Ended December 31,

	2009	2008
		(Restated)
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (3,058,000)	(16,874,000)
Adjustments to Reconcile Net Loss to Net		
Cash used in Operating Activities		
Depreciation and amortization of property and equipment	1,910,000	1,490,000
Loss on disposition of property and equipment	22,000	-
Amortization of intangible assets	183,000	221,000
Amortization of capitalized engineering costs	856,000	551,000
Bad debt expense	80,000	135,000
Non-cash compenstion expense	102,000	237,000
Non-Cash Share Payment	-	81,000
Non-Cash Interest Expense Including Amortization of Debt Discounts	3,092,000	594,000
Amortization of deferred financing costs	266,000	297,000
Gain on Sale of Real Estate	(38,000)	(38,000)
Deferred Income Taxes	(1,364,000)	(515,000)
Deferred Rent	190,000	190,000
Lease Impairment	579,000	-
Loss on Impairment	-	9,410,000
Changes in Assets and Liabilities		
(Increase) Decrease in Operating Assets:		
Accounts Receiveable	(376,000)	(229,000)
Assets Held for Sale	1,308,000	5,186,000
Inventory	(469,000)	(2,859,000)
Prepaid Expenses and Other Current Assets	(120,000)	77,000
Deposits	6,000	805,000
Other Assets	51,000	144,000
Increase (Decrease) in Operating Liabilities		
Accounts payable and accrued expenses	851,000	26,000
Income Taxes payable	4,000	(198,000)
Liabilities Held For Sale	(785,000)	1,084,000
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	3,290,000	(185,000)
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash paid for Capitalized Engineering costs	(511,000)	(1,062,000)
Purchase of property and equipment	(1,207,000)	(1,456,000)
Assets Held for Sale	-	(256,000)
NET CASH USED IN INVESTING ACTIVITIES	(1,718,000)	(2,774,000)
CASH FLOWS FROM FINANCING ACTIVITIES		
Notes payable - Sellers	(234,000)	(961,000)
Capital lease obligations	(338,000)	(346,000)
Notes payable-Jr. Subordinated Debt	445,000	5,545,000
Notes payable-SFFC	(40,000)	-
Notes payable-Revolver	(761,000)	(553,000)
Notes payable-Bank	(518,000)	(138,000)
Cash paid for deferred financing costs	(125,000)	(424,000)
NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES	(1,571,000)	3,123,000
Net increase in cash and cash equivalents	1,000	164,000
Cash and cash equivalents at beginning of year	164,000	-
Cash and cash equivalents at end of year	165,000	164,000
Supplemental cash flow information		
Cash paid during the year for interest	$ 2,044,000	$ 1,969,000
Supplemental cash flow information		
Cash paid during the year for Income taxes	$ -	$ -
Supplemental schedule of non-cash investing and financing activities		
Property and equipment acquired under capital leases	$ 196,000	$ 827,000
Non-cash dividends on Series B Preferred Stock	$ 1,431,000	$ 620,000
Issuance of common stock in settlement of vendor payables	$ 43,000	$ -
Issuance of Series B Preferred Stock in settlement of vendor payables	$ 125,000	$ -
Reversal of dividends payable of Series A Preferred Stock	$ 120,000	$ -
Issuance of Series B Preferred Stock in settlement of notes payable - sellers	$ 597,000	$ -

See notes to consolidated financial statements

Note 1. FORMATION AND BASIS OF PRESENTATION

Merger and Acquisition

Ashlin Development Corp. (the "Company" or "Ashlin"), a Florida corporation, entered into a Merger Agreement on November 14, 2005 with Gales Industries Incorporated, a privately-held Delaware corporation ("Original Gales"). As a result of the transaction, the former stockholders of Original Gales became the controlling stockholders of Ashlin. Additionally, since Ashlin had no substantial assets prior to the merger, the transaction was treated for accounting purposes as a reverse acquisition of a public shell. Accordingly, for financial statement presentation purposes, Original Gales is the surviving entity.

Prior to the closing of the merger, Original Gales acquired all of the outstanding capital stock of Air Industries Machining Corporation ("AIM"). Because of the change in ownership, management and control that occurred in connection with the acquisition of AIM by Original Gales, the transaction was accounted for as a purchase.

Original Gales was formed in October 2004. Prior to the acquisition of AIM, Original Gales did not have any business operations or activity other than the transactions contemplated with the merger and succeeded to substantially all of the business operations of AIM. As such, AIM is the "Predecessor" to Original Gales.

On February 15, 2006, Ashlin changed its name to Gales Industries Incorporated and its state of domicile from Florida to Delaware. On June 26, 2007, the name of the Company was changed from Gales Industries Incorporated to Air Industries Group, Inc.

The financial statements presented are those of Original Gales, now known as Air Industries Group, Inc. ("AIRI") and its wholly-owned subsidiaries; AIM, Sigma Metals Inc. (discontinued as of October 31, 2008) ("Sigma") and Welding Metallurgy, Inc. ("Welding"). See Note 2 Acquisitions and Dispositions.

At a Special Meeting of Stockholders on July 29, 2010, the stockholders approved an amendment to the certificate of incorporation to effect a one-for-four hundred (1-for-400) reverse split of our common stock. All share figures and results are reflected on a post-split basis.

Basis of Presentation

The Company is highly leveraged and will need to generate substantial cash flow from operations to satisfy its debt service obligations. As of December 31, 2009, the Company's gross indebtedness was approximately $25,138,000, including approximately $14,478,000 payable to its bank lenders secured by substantially all its assets. Because the Company is required to maintain a "lock box" account with PNC Bank N.A. into which substantially all of the Company's cash receipts are paid, if its bank lenders were to cease lending, the Company would lack the funds to continue its operations. The Company's bank debt matured in April 2010. The lenders agreed to extend the maturity of the loans to August 2010. These loans were then subsequently extended to October 15, 2010 and again until November 15, 2010. On November 30, 2010, the Company refinanced its bank debt with PNC Bank N.A. for a term of three years. See Note 9 Notes Payable and Capital Lease Obligations.

To alleviate its liquidity difficulties, during 2009, the Company sold certain of the assets and the operations of its Sigma business and extended the payment terms of its indebtedness to the former owners of Welding. In addition, the Company received gross proceeds from the sale of its junior subordinated notes and equity securities of $5,990,000 between May 2008 and March 2009.

To preserve its liquidity, the Company issued additional shares of its Series B Convertible Preferred Stock ("Series B Preferred") in lieu of payment of cash dividends on its Series B Preferred. This diluted the equity ownership and voting power of holders of its Common Stock. See Note 10 Stockholders' Equity.

Nevertheless, the ability of the Company to maintain its current level of operations is subject to the cooperation of PNC Bank N.A. and other parties which hold its notes. If PNC Bank N.A. was to reduce the amounts loaned to the Company, the Company would have no choice other than to reduce it operations and seek to liquidate certain assets. Any forced liquidation of assets would likely yield less than the amounts at which such assets are valued by the Company.

Restatement

The 2008 financial statements were restated for the following:

During the preparation of the Company's December 31, 2009 consolidated financial statements, we discovered that certain expenses in the amount of $286,000 which should have been included in cost of goods sold were classified as a reduction of accounts payable and accrued expenses, resulting in the understatement of cost of goods sold and accounts payable and accrued expenses by a like amount. Additionally, $45,000 was capitalized as property and equipment that should have been included as part of cost of goods sold. This resulted in an overstatement of property and equipment and an understatement of cost of goods sold by a like amount.

As a result of the restatement, net loss attributable to common stockholders for the year ended December 31, 2008 increased by $331,000 ($1.88 per share). Stockholders' equity decreased by a like amount.

The balance sheet accounts affected by the restatement are as follows at December 31, 2008:

	As Originally Reported	Adjustments	As Restated
Property and Equipment	$ 5,507,000	$ (45,000)	$ 5,462,000
Accounts Payable and Accrued Expenses	5,167,000	286,000	5,453,000
Accumulated Deficit	$(17,428,000)	$ (331,000)	$ (17,759,000)

Note 2. ACQUISITIONS AND DISPOSITIONS

Sigma

On April 16, 2007, the Company purchased all of the outstanding capital stock of Sigma for approximately $7,500,000.

During 2008, Sigma's results began to deteriorate and we concluded that to revive the business would require a significant investment. Therefore, in the third quarter of 2008, the Board of Directors decided to discontinue the operations of Sigma. Operations were discontinued on October 31, 2008. The Company's financial statements reflect Sigma as discontinued operations. The results of operations of this entity is treated as (loss) income from discontinued operations, net of tax and separately stated on the Consolidated Statements of Operations below loss from continuing operations. See Note 16 Discontinued Operations. Sigma's assets and liabilities were classified as held for sale on the Company's consolidated balance sheet for all periods presented.

The Company reached an agreement to sell certain assets of the business to the former stockholders of Sigma in October 2008. In January 2009, the sale was closed. The Company sold assets including certain accounts receivable, property and equipment, customer list and the rights, title and interest in the name Sigma Metals, Inc. and the domain name Sigmametalsinc.com. In connection with the sale, the Company and the former stockholders of Sigma consummated a Settlement Agreement in which the balances due under the notes issued for the Company's acquisition of Sigma were converted into 58,500 shares of the Company's Series B Preferred. See Note 10 Stockholders' Equity. In addition, the employment agreements entered into by the former stockholders of Sigma were terminated. See Note 12 Commitments and Contingencies.

Welding

On August 24, 2007, the Company acquired all of the issued and outstanding capital stock of Welding pursuant to a Stock Purchase Agreement, dated as of March 9, 2007. The acquisition was financed by Steel City Capital Funding LLC and a stockholder of Welding. See Note 9 Notes Payable and Capital Lease Obligations. Welding is a specialty welding and products provider whose significant customers include the world's largest aircraft manufacturers, subcontractors, and original equipment manufacturers.

Note 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Adoption of FASB Accounting Standards Codification

Effective July 1, 2009, the Financial Accounting Standards Board's (“FASB”) Accounting Standards Codification ("ASC") became the single official source of authoritative, nongovernmental generally accepted accounting principles (“GAAP”) in the United States. The historical GAAP hierarchy was eliminated and the ASC became the only level of authoritative GAAP, other than guidance issued by the Securities and Exchange Commission. Our accounting policies were not affected by the conversion to ASC. However, references to specific accounting standards in the footnotes to our consolidated financial statements have been changed to refer to the appropriate section of ASC.

Principal Business Activity

The Company is primarily engaged in manufacturing aircraft structural parts, and assemblies for prime defense contractors in the aerospace industry in the United States. The Company's customers consist mainly of publicly- traded companies in the aerospace industry.

Principles of Consolidation

The accompanying consolidated financial statements include accounts of the Company and its wholly-owned subsidiaries, AIM and Welding. Significant inter-company accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid instruments with an original maturity of three months or less.

Accounts Receivable

Accounts receivable are reported at their outstanding unpaid principal balances net of allowances for uncollectable accounts. The Company provides for allowances for uncollectible receivables based on management's estimate of uncollectible amounts considering age, collection history, and any other factors considered appropriate. The Company writes off accounts receivable against the Allowance for Doubtful Accounts when a balance is determined to be uncollectible.

Inventory Valuation

The Company values inventory at the lower of cost on a first-in-first-out basis or market.

AIM generally purchases inventory only when it has non-cancellable contracts from its customers for orders of its finished goods. Welding Metallurgy generally produces pursuant to customer orders and maintains relatively low inventory levels. AIM occasionally produces finished goods in excess of purchase order quantities in anticipation of future purchase order demand; historically this excess has been used in fulfilling future purchase orders. The Company periodically evaluates inventory items that are not secured by purchase orders and establishes reserves for obsolescence accordingly. The Company also reserves for excess quantities, slow-moving goods, and for other impairment of value.

Capitalized Engineering Cost

The Company has contractual agreements with customers to produce parts, which the customers design. Though the Company has not designed and thus has no proprietary ownership of the parts, the manufacturing of these parts require pre-production engineering and programming of our machines. The pre-production costs associated with a particular contract are capitalized and then amortized beginning with the first shipment of product pursuant to such contract. These costs are amortized on a straight line basis over the estimated length of the contract, or if shorter, three years.

If the Company is reimbursed for all or a portion of the pre-production expenses associated with a particular contract, only the unreimbursed portion would be capitalized. The Company may also progress bill customers for certain engineering costs being incurred. Such billings are recorded as progress billings (a reduction of the associated inventory) until the appropriate revenue recognition criteria have been met. The Terms and Conditions contained in customer purchase orders may provide for liquidated damages in the event that a stop-work order is issued prior to the final delivery of the product.

Property and Equipment

Property and equipment are carried at cost net of accumulated depreciation and amortization. Repair and maintenance charges are expensed as incurred. Property, equipment, and improvements are depreciated using the straight-line method over the estimated useful lives of the asset or the particular improvement. Expenditures for repairs and improvements in excess of $1,000 that add to the productive capacity or extend the useful life of an asset are capitalized. Upon disposition, the cost and related accumulated depreciation are removed from the accounts and any related gain or loss is reflected in earnings.

Long-Lived and Intangible Assets

Identifiable intangible assets are amortized using the straight-line method over the period of expected benefit.

Long-lived assets and intangible assets subject to amortization to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the related carrying amount may be impaired. The Company records an impairment loss if the undiscounted future cash flows are found to be less than the carrying amount of the asset. If an impairment loss has occurred, a charge is recorded to reduce the carrying amount of the asset to fair value. There has been no impairment for the years 2009 or 2008.

Deferred Financing Costs

Costs incurred with obtaining and executing debt arrangements are capitalized and amortized on the effective interest method over the term of the related debt.

Revenue Recognition

The Company recognizes revenue in accordance with Staff Accounting Bulletin No. 104, "Revenue Recognition." The Company recognizes revenue when products are shipped and the customer takes ownership and assumes risk of loss, collection of the relevant receivable is probable, persuasive evidence of an arrangement exists, and the sales price is fixed or determinable. Payments received in advance from customers for products delivered are recorded as customer advance payments until earned, at which time revenue is recognized. The Terms and Conditions contained in our customer Purchase orders often provide for liquidated damages in the event that a stop work order is issued prior to the final delivery. The Company utilizes a Returned Merchandise Authorization or RMA process for determining whether to accept returned products. Customer requests to return products are reviewed by the contracts department and if the request is approved, a credit is issued upon receipt of the product. Net sales represent gross sales less returns and allowances. Shipping costs are included in cost of sales.

Use of Estimates

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts in the financial statements and accompanying notes. The more significant management estimates are the useful lives of property and equipment, provisions for inventory obsolescence, accrued expenses and various contingencies. Actual results could differ from those estimates. Changes in facts and circumstances may result in revised estimates, which are recorded in the period in which they become known.

Credit and Concentration Risks

There were three customers that represented $ 33,787,000 or 75.0 % of the net sales for the year ended December 31, 2009 and $27,899,000 or 71.3 % for the year ended December 31, 2008. One customer accounted for 47.6% and 48.7% of net sales for the year ended December 31, 2009 and 2008, respectively. Sales to this customer are subject to General Ordering Agreements which extend through 2013. Amounts receivable from this customer at December 31, 2009 and 2008 were $1,082,000 or 20.7% and $525,000 or 9.6% of net accounts receivable, respectively. The second customer accounted for 18.4% and 11.9% of sales for 2009 and 2008, respectively, and $1,816,000 or 34.7% and $1,296,000 or 23.7% of net accounts receivable at December 31, 2009 and 2008, respectively. The third customer represented 9.0% and 10.7% of sales at December 31, 2009 and 2008, respectively, and $459,000 or 8.8% and $1,275,000 or 23.2% of the net accounts receivable at December 31, 2009 and 2008, respectively.

During the year, the Company had occasionally maintained balances in its bank accounts that were in excess of the FDIC limit. The Company has not experienced any losses on these accounts.

Substantially all of the workforce at AIM are subject to a union contract with the United Service Workers Union TUJAT Local 355 (the "Union"). The contract is scheduled to expire on December 31, 2011.

AIM has several key sole-source suppliers of various parts that are important for one or more of our products. These suppliers are our only source for such parts and, therefore, in the event any of them were to go out of business or be unable to provide us parts for any reason, our business could be severely harmed.

Fair Value of Financial Instruments

The Company has estimated the fair value of financial instruments using available market information and other valuation methodologies. Management of the Company believes that the fair value of financial instruments, consisting of cash, accounts receivable, accounts payable and accrued liabilities, approximates carrying value due to the immediate or short-term maturity associated with these instruments and that the notes payable approximate fair value in that they carry market-based interest rates.

Income Taxes

The Company accounts for income taxes in accordance with accounting guidance now codified as FASB ASC 740, "Income Taxes," which requires that the Company recognize deferred tax liabilities and assets based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities, using enacted tax rates in effect in the years the differences are expected to reverse. Deferred income tax benefit (expense) results from the change in net deferred tax assets or deferred tax liabilities. A valuation allowance is recorded when it is more likely than not that some or all deferred tax assets will not be realized.

The Company has adopted the provisions of FASB ASC 740-10-05 "Accounting for Uncertainty in Income Taxes." The ASC clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements. The ASC prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The ASC provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

Earnings per share

Basic earnings per share is computed by dividing the net income applicable to common stockholders by the weighted-average number of shares of common stock outstanding for the period. Potentially dilutive shares, using the treasury stock method, are included in the diluted per-share calculations for all periods when the effect of their inclusion is dilutive.

The Company did not include 20,207 warrants and 15,930 options to purchase the Company's common stock for the year ended December 31, 2009 and 32,328 warrants and 16,307 options to purchase the Company's common stock for the year ended December 31, 2008 in the calculation of diluted earnings per share because the effects of their inclusion would have been anti-dilutive. The shares of Series B Preferred that are convertible into 238,796 shares of common stock at December 31, 2009 and 126,064 at December 31, 2008 are not included in the calculation of diluted earnings per shares because the effect of the inclusion would have been anti-dilutive.

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with FASB ASC 718, "Compensation – Stock Compensation." Under the fair value recognition provision of the ASC, stock-based compensation cost is estimated at the grant date based on the fair value of the award. The Company estimates the fair value of stock options and warrants granted using the Black-Scholes-Merton option pricing model.

Goodwill

Goodwill represents the excess of the acquisition cost of businesses over the fair value of the identifiable net assets acquired. Goodwill is not amortized, but is tested at least annually for impairment, or if circumstances change that will more likely than not reduce the fair value of the reporting unit below its carrying amount. .The Company performs impairment testing for goodwill annually, or more frequently when indicators of impairment exist, using a two-step approach. Step one compares the fair value of the net assets of the relevant reporting unit (calculated using a discounted cash flow method) to its carrying value, a second step is performed to compute the amount of the impairment. In this process, a fair value for goodwill is estimated, based in part on the fair value of the operations, and is compared to its carrying value. The shortfall of the fair value below carrying value represents the amount of goodwill impairment.

As more fully described in Note 7 Goodwill, during the year ended December 31, 2008, the Company recorded an impairment charge of $4,532,000 related to goodwill. The Company has determined that there has been no impairment during 2009.

Recently Issued Accounting Standards

In October 2009, the FASB issued new standards for revenue recognition with multiple deliverables. These new standards impact the determination of when the individual deliverables included in a multiple-element arrangement may be treated as separate units of accounting. Additionally, these new standards modify the manner in which the transaction consideration is allocated across the separately identified deliverables by no longer permitting the residual method of allocating arrangement consideration. These new standards are effective for us beginning in the first quarter of fiscal year 2011, however early adoption is permitted. We do not expect these new standards to significantly impact our consolidated financial statements

In October 2009, the FASB issued new standards for the accounting for certain revenue arrangements that include software elements. These new standards amend the scope of pre-existing software revenue guidance by removing from the guidance non-software components of tangible products and certain software components of tangible products. These new standards are required to be adopted in the first quarter of 2011; however, early adoption is permitted. We do not expect these new standards to significantly impact our consolidated financial statements.

In January 2010, the FASB issued amended standards that require additional fair value disclosures. These amended standards require disclosures about inputs and valuation techniques used to measure fair value as well as disclosures about significant transfers, beginning in the first quarter of 2010. Additionally, these amended standards require presentation of disaggregated activity within the reconciliation for fair value measurements using significant unobservable inputs (Level 3), beginning in the first quarter of 2011. We do not expect these new standards to significantly impact our consolidated financial statements.

In February 2010, the Financial Accounting Standards Board issued an amendment to accounting standards related to subsequent events. The amendment exempts Securities and Exchange Commission registrants from the requirement to disclose the date through which it has evaluated subsequent events for either original or restated financial statements. The standard is effective February 2010. The Company adopted this standard in February 2010. The adoption did not impact the Company’s consolidated financial position or results of operations, other than additional reporting requirements.

In April 2010, the FASB issued Accounting Standards Update 2010-17 (ASU 2010-17), “Revenue Recognition-Milestone Method (Topic 605): Milestone Method of Revenue Recognition.” The amendments in this Update are effective on a prospective basis for milestones achieved in fiscal years, and interim periods within those years, beginning on or after June 15, 2010. The adoption of the provisions of ASU 2010-17 did not have a material effect on the financial position or results of operations of the Company.

Management does not believe that any other recently issued, but not yet effective, accounting standard if currently adopted would have a material effect on the accompanying financial statements.

Subsequent Events

Management has evaluated subsequent events through December 21, 2010, the date at which the financial statements were available to be issued.

Note 4. INVENTORY

The components of inventory consisted of the following:

	2009	2008 (Restated)
Raw Materials	$ 8,066,000	$ 6,809,000
Work In Progress	8,898,000	9,633,000
Finished Goods	5,350,000	5,224,000
Inventory Reserve	(746,000)	(567,000)
Total Inventory	$ 21,568,000	$ 21,099,000

Note 5. PROPERTY AND EQUIPMENT, NET

The components of property and equipment consisted of the following:

	2009	2008 (Restated)	
Machinery and Equipment	$3,267,000	$3,083,000	5 - 8 years
Capital Lease Machinery and Equipment	2,695,000	2,499,000	5 - 8 years
Tools and Instruments	2,827,000	1,871,000	1.5 - 7 years
Automotive Equipment	55,000	30,000	5 years
Furniture and Fixtures	193,000	194,000	5 - 8 years
Leasehold Improvements	548,000	549,000	Term of Lease
Computers and Software	141,000	142,000	4-6 years
Total Property and Equipment	9,726,000	8,368,000	
Less: Accumulated Depreciation	(4,793,000)	(2,906,000)	
Property and Equipment, net	$4,933,000	$5,462,000	

Depreciation and amortization expense for the years ended December 31, 2009 and 2008 were approximately $1,910,000 and $1,490,000, respectively.

Note 6. INTANGIBLE ASSETS, NET

The components of the intangibles assets are comprised of the following:

	2009	2008 (Restated)	
Customer Relationships	$ 890,000	$ 890,000	11 to 14 years
Trade Names	770,000	770,000	20 years
Technical Know-how	660,000	660,000	10 years
Professional Certifications	114,000	114,000	.25 to 2 years
Total Intangible Assets	2,434,000	2,434,000	
Less: Accumulated Amortization	491,000	308,000	
Intangible Assets, net	$1,943,000	$2,126,000	

The expense for the amortization of the intangibles for the years ended December 31, 2009 and 2008 were $183,000 and $221,000, respectively.

Future amortization of intangibles is as follows:

Year	Amount
2010	$ 168,000
2011	168,000
2012	168,000
2013	168,000
2014	168,000
Thereafter	1,103,000
Total	$1,943,000

Note 7. GOODWILL

Goodwill of $3,556,000 was recorded in connection with the acquisition of Welding and consists of the cost over the fair value of net assets (see Note 2 Acquisitions). Additionally, goodwill in the amount of $1,266,000 was recorded in connection with the acquisition of AIM. During the annual testing for the impairment of goodwill, it was determined that there was no impairment during the year ended December 31, 2009. During the annual testing for the year ended December 31, 2008, it was determined that the Company should reduce the value of the recorded goodwill on AIM to $0 and the value recorded on Welding to $291,000. The basis for this impairment was due to liquidity constraints and the results of operations during the year ended December 31, 2008. Therefore, an impairment charge of $4,532,000 was recognized in the Consolidated Statement of Operations for the year ended December 31, 2008.

Note 8. SALE AND LEASEBACK TRANSACTION

On October 24, 2006, the Company consummated a Sale & Leaseback Arrangement, whereby the Company sold the buildings and real property comprising its corporate headquarters in Bay Shore, New York (the "Property") for a purchase price of $6,200,000. The Company accounted for the transaction under the provisions of FASB ASC 840-40, “Leases – Sale-Leaseback Transactions.” As a result, the Company realized a gain on the sale of $1,051,000 of which we recognized $300,000 during the year ended December 31, 2006. The remaining $751,000 is being recognized ratably over the remaining term of the twenty year lease at approximately $38,000 per year. The gain is included in Other Income in the accompanying Consolidated Statement of Operations. The unrecognized portion of the gain in the amount of $599,000 and $637,000 as of December 31, 2009 and 2008, respectively, is classified as Deferred Gain on Sale in the accompanying Consolidated Balance Sheet.

Simultaneous with the closing of the sale of the Property, the Company entered into a 20-year triple-net lease (the "Lease") with the Purchaser for the property. Base annual rent is approximately $540,000 for the first five years, $560,000 for the sixth year, and thereafter increases 3% per year. The Lease grants AIM an option to renew the Lease for an additional period of five years. The Company deposited with the Purchaser $127,500 as security for the performance of its obligations under the Lease, which it subsequently replaced with a $127,500 letter of credit. In addition, the Company deposited with the landlord $393,000 as security for the completion of certain repairs and upgrades to the Property. In April 2010, the Company replaced the letter of credit with a cash deposit. This amount is included in the caption Deferred Finance costs, net, Deposit and Other Assets on the accompanying Consolidated Balance Sheet. Pursuant to the terms of the Lease, the Company is required to pay all of the costs associated with the operation of the facilities, including, without limitation, insurance, taxes and maintenance. These costs will be offset against the funds that are deposited with the landlord. The lease also contains customary representations, warranties, obligations, conditions and indemnification provisions and grants the Purchaser customary remedies upon a breach of the lease by the Company, including the right to terminate the Lease and hold the Company liable for any deficiency in future rent. See Note 12 Commitments and Contingencies.

Note 9. NOTES PAYABLE AND CAPITAL LEASE OBLIGATIONS

Notes payable and capital leases obligations consist of the following:

	2009	2008 (Restated)
Revolving credit notes payable to PNC Bank N.A. ("PNC") and secured by substantially all assets	$ 10,018,000	$ 10,779,000
Term loan, subject to acceleration, secured	4,460,000	4,500,000
Junior subordinated notes	6,500,000	6,055,000
Notes payable to sellers of acquired businesses	2,284,000	3,071,000
Capital lease obligations	1,876,000	1,960,000
Other notes payable to PNC, secured	-	518,000
Subtotal	25,138,000	26,883,000
Less: Current portion of notes and capital obligations	20,711,000	16,904,000
Unamortized debt discount on junior subordinated notes	1,323,000	4,006,000
Notes payable and capital lease obligations, net of current portion	$ 3,104,000	$ 5,973,000

PNC Bank N.A. ("PNC")

On November 30, 2005, the Company executed a credit facility with PNC (the "Loan Facility"), secured by substantially all of its assets. The Loan Facility provided for maximum borrowings of $19,000,000 consisting of the following:

(i) a $14,000,000 revolving loan
(ii) a $3,500,000 term loan and
(iii) a $1,500,000 equipment financing loan

On November 30, 2010, the Company executed an amendment to the Loan Facility with PNC providing for the following:

(i) a $16,000,000 revolving loan
(ii) a $3,000,000 term loan and
(iii) included Welding Metallurgy as one of the borrowers

The revolving loan originally bore interest, at the option of the Company, that is based on (i) the higher of (A) PNC's base commercial lending rate as published from time to time ("PNC Rate") plus 0.25% or (B) the Federal Funds rate plus 0.5%, or (ii) the Eurodollar Rate for the Interest Period selected by the Company plus 2.5%.The revolving loan had an interest rate of 5.50% and 6.25% per annum at December 31, 2009 and 2008, respectively, and an outstanding balance of $ 10,018,000 and $10,779,000, respectively. The revolving loan was payable in full in April 2010 but the maturity date was extended as discussed below. The interest rates were amended as part of the Ninth Amendment to the Loan Facility (see discussion below).

Each day, the Company's cash collections (except for Welding) are swept directly by the bank to reduce the revolving loans and we then borrow according to a borrowing base. As such, the Company generally has no cash on hand. Because the revolving loans contain a subjective acceleration clause which could permit PNC to require repayment prior to maturity, the loans are classified with current portion of notes and capital lease obligations.

The original term loan was for a period of four (4) years and bore interest, at the option of the Company, at the (i) PNC Rate plus 0.50% per annum or (ii) the Eurodollar Rate for the interest period selected by the Company plus 2.75 %. In October 2006, the Term Note was reduced by a payment of $2,800,000 and an Amended and Restated Term Note in the amount of $383,330 was issued providing for principal payments of $10,648 per month. The maturity date was extended to become the first business day of October 2009. At December 31, 2009 and 2008, the balance of the term loan was $0 and $107,000, respectively.

The new term loan in the amount of $3,000,000 matures in December 2013 and bears interest, at the option of the Company equal to (a) the greater of (i) the sum of the PNC Rate plus 6.5% and (ii) 11.5%, with respect to Domestic Rate Loans or (b) the greater of (i) the sum of the Eurodollar Rate plus 8.5% and (ii) 10.5%, with respect to Eurodollar Rate Loans. Repayment under the term loan shall consist of 36 consecutive monthly principal installments, the first 35 of which will be in the amount of $83,330 commencing on the first business day of January 2011, with the 36th and final payment of any unpaid balance of principal and interest payable on the first business day of December 2013. Additionally, there is a mandatory prepayment of equal to 50% of Excess Cash Flow (as defined) for each fiscal year commencing with the fiscal year 2011, payable upon the delivery of the financial statements to PNC for such fiscal period, but no later than 90 days after the end of the fiscal year. The proceeds of this term loan were used to repay the balance due Steel City Capital Funding LLC (see below).

In addition to the foregoing, the Loan Facility was further amended to allow the Company to borrow or to obtain the issuance, renewal, extension and increase of standby letters of credit, up to an aggregate availability of $500,000, for its account until November 30, 2009. At both December 31, 2009 and 2008, the Company had an outstanding letter of credit in the amount of $127,500. In April 2010, the Letter of Credit was replaced with a cash deposit.

The equipment loans bore interest, at the option of the Company, that is based on (i) the PNC Rate plus 0.50% per annum or (ii) the Eurodollar Rate for the interest period selected plus 2.75% per annum. The equipment loan had an interest rate of 7.75% per annum at December 31, 2008. Such equipment financing is limited to an aggregate of $750,000 in any fiscal year and amortized in equal installments of sixty months following the close of each "borrowing period", the first of which ended December 31, 2007. Each subsequent "borrowing period" ends on each December 31 thereafter. All equipment loans were due and payable on April 30, 2010. As part of the Ninth Amendment to the Loan Facility, the availability block was reduced to allow this loan to be paid in full. At each of December 31, 2009 and 2008, the equipment financing loan had a balance of $0 and $411,000, respectively.

To the extent that the Company may dispose of collateral used to secure the Loan Facility, other than inventory, the Company must promptly repay the draws on the credit facility in amount equal to the net proceeds of such sale.

The terms of the Loan Facility require that, among other things, the Company maintain certain financial ratios and levels of working capital. As of December 31, 2009 and 2008, the Company had not met these terms and was in default. Such defaults were waived as part of the Eleventh and Ninth Amendment to the Loan Facility, respectively (see discussion below).

The Loan Facility also is secured by all assets of the Company and the Company's receivables are payable directly into a lockbox controlled by PNC (subject to the terms of the Loan Facility). PNC may use some elements of subjective business judgment in determining whether a material adverse change has occurred in the Company's condition, results of operations, assets, business, properties or prospects allowing it to demand repayment of the Loan Facility.

The Company executed Amendments Six to Fourteen to the Loan Facility during the years 2009 and 2010. These Amendments included the following:

- Waived prior defaults
- Amended the financial ratios
- Amended the formula to determine the amounts of revolving advances permitted to be borrowed under the Loan Facility.
- Reduced the availability reserve so that the excess availability created by the reduction will be utilized to payoff in full the term loan and equipment loans.
- Amended the revolving interest rate to (a) the sum of PNC Rate plus 2.25% or (b) the greater of (i) the sum of the Eurodollar rate plus 3.5% and (ii) 5.5%.
- The Company paid amendment fees ranging from $10,000 to $25,000.

Effective November 30, 2010, the Fifteenth Amendment to the Loan Facility was signed. The terms of the Fifteenth Amendment included the following:

- Waived prior defaults
- Extended the due date of the Loan Facility to November 15, 2013
- Amend the financial ratios
- Increase the inventory sub-limit to $11,250,000
- Increase the Maximum Revolving advance to $16,000,000
- Include Welding Metallurgy as a borrower under the revolving portion of the Loan Facility
- Include a term loan in the amount of $3,000,000 (discussed above)
- The Company paid an amendment fee of $95,000.

Steel City Capital Funding LLC ("SCCF")

In connection with the Welding acquisition, SCCF provided a Term Loan (the "SCCF Loan Agreement") of $4,500,000, which was originally payable on August 24, 2010. Borrowings under the SCCF Loan Agreement originally bore interest, payable monthly, generally at a rate of 6% over the base commercial lending rate of PNC as publicly announced to be in effect from time to time. The interest rate on the outstanding indebtedness under the SCCF Loan Agreement was approximately 10.75% and 9.25% for the years ended December 31, 2009 and 2008, respectively. At December 31, 2009 and 2008, the balance owed on the SCCF Loan Agreement amounted to $4,460,000 and $4,500,000, respectively.

On January 29, 2009, SCCF notified the Company of a default of covenants under the SCCF Loan Agreement, and subsequently imposed a default rate of interest of 13.25% as of April 6, 2009. Such defaults were waived as part of the Fourth Amendment to the SCCF Loan Agreement (see discussion below).

The Company executed Amendments Four through Eight to the SCCF Loan Agreement during the years 2009 and 2010. These Amendments included the following :

- Waived prior defaults
- Amended the financial ratios and now includes all entities (except Sigma) in the calculations
- Amended the interest rate to (a) the sum of (i) the greater of (1) PNC Rate or (2) 4.75% plus (ii) 6% for domestic loans and (b) the sum of (i) the greater of (1) the Eurodollar Rate or (2) 2.25% plus (ii) 8.5% for Eurodollar Rate loans.
- Prohibited cash payments to vendors of Sigma in excess of $150,000 in the aggregate during each of (i) the period September 1, 2009 through December 31, 2009, and (ii) each calendar year commencing January 1, 2010.
- The Company paid amendment fees of ranging from $10,000 to $50,000.

To secure payment of the indebtedness under the SCCF Loan Agreement, AIRI pledged all of the outstanding shares of AIM and Sigma, which, in turn, pledged all of the outstanding shares of Welding. Such security, though, is subordinate to PNC.

On November 30, 2010, the Company entered into an amendment of the credit facility with PNC. Under the terms of that amendment, SCCF was paid in full. This payment was funded by the proceeds of the $3,000,000 term loan with PNC as well as with proceeds from the revolving line of credit. The Company paid a fee of $10,000 to SCCF to terminate the SCCF Loan Agreement.

Interest expense related to these credit facilities amounted to approximately $1,112,000 and $1,262,000 for the years ended December 31, 2009 and 2008, respectively.

Future minimum principal payments of the new PNC term loan are as follows:

Year	Amount
2010	$ -
2011	1,000,000
2012	1,000,000
2013	1,000,000
PNC Term Loan Payable	3,000,000
Less: Current portion	-
Long-term portion	$ 3,000,000

Capital Leases Payable – Equipment

The Company was committed under several capital leases for manufacturing and computer equipment. All leases had bargain purchase options exercisable at the termination of each lease. On April 28, 2009, the Company refinanced and consolidated its existing capital leases into one new five-year capital lease. The monthly payment was reduced to $38,000 from an average of $52,000 under the previous leases. Additionally, the Company entered into three new capital leases in 2009. Capital lease obligations totaled $1,876,000 and $1,960,000 as of December 31, 2009 and 2008, respectively, with various interest rates ranging from 7.7% to 9.5%.

As of December 31, 2009, the aggregate future minimum lease payments, including imputed interest, with remaining terms of greater than one year are as follows:

Year	Amount
2010	$ 503,000
2011	503,000
2012	503,000
2013	503,000
2014	218,000
Total future minimum lease payments	2,230,000
Less: imputed interest	(354,000)
Less: current portion	(368,000)
Total Long Term Portion	$1,508,000

Notes Payable - Sellers

As of December 31, 2009 and 2008, the balances owed to the sellers by acquisition are:

		2009		2008 (Restated)
AIM	$	240,000	$	433,000
Sigma		-		638,000
Welding		2,044,000		2,000,000
Subtotal	$	2,284,000	$	3,071,000
Less: Current Portion		688,000		1,053,000
Total long-term portion	$	1,596,000	$	2,018,000

AIM

On November 30, 2005, in connection with the acquisition of AIM, the Company issued notes payable for an aggregate of $1,627,000 to three former AIM shareholders, two of whom have remained as part of the Company's senior management and are also stockholders of the Company.

The balance owed at December 31, 2009 and 2008 amounted to $288,700 and $433,000, respectively and matures on September 30, 2010. The remaining balance is subordinated to all of the Company's PNC senior debt and is payable in twenty consecutive calendar quarters of equal installments of $48,100 principal plus accrued interest. The interest rate on this note is equal to Prime Rate plus 0.5% per annum (3.75% and 3.75% at December 31, 2009 and 2008, respectively). Interest on outstanding balances at September 30, 2010, in the event of nonpayment, shall accrue at a floating rate equal to the Prime Rate plus 7% per annum.

Sigma

In connection with the acquisition of Sigma, the Company incurred notes payable obligations to the former stockholders of Sigma. At December 31, 2008, the remaining principal balance totaled $638,000. The amount is classified as part of Liabilities Held for Sale on the Consolidated Balance Sheet. These notes were subordinated to all of the Company's indebtedness to PNC and SCCF.

In January 2009, as part of the sale of Sigma to its former stockholders, such stockholders and the Company consummated a Settlement Agreement in which these notes were converted into 58,500 shares of Series B Preferred. See Note10 Stockholders' Equity and Note 16 Discontinued Operations.

Welding

In connection with the acquisition of Welding, the Company incurred a note payable to the former stockholders of Welding in the aggregate principal amount of $2,000,000, which bore no interest until August 24, 2008, and then at 7% per annum ("Old Note"). To reflect the fact that this note did not bear interest for the first year, we discounted the value of the note and expensed the imputed interest monthly accreting up the value of the note to its face value of $2,000,000 in August 2008.

In August 2008, the Company and the former stockholders reached an agreement restructuring the Company’s obligation under this note by executing an Amended and Restated Subordinated Promissory Note, the “New Note”. The principal balance of this New Note was $2,050,000 (consisting of $2,000,000 principal amount of the promissory note dated August 25, 2007, plus an unpaid working capital adjustment in the amount of $50,000), Payments due under the New Note are: $25,000 principal on each of October

31, 2008 and December 31, 2008, an additional $50,000 on March 31, 2009, followed by 19 equal consecutive quarterly installments of $100,000, commencing on June 30, 2009 and continuing through December 31, 2013, payable on the last business day of each March, June, September and December, commencing June 30, 2009 and continuing through and including December 31, 2013, with one final payment of $50,000 on March 31, 2014, plus accrued interest thereon at the rate of 7% per annum from August 28, 2008.

As additional consideration, the former stockholders were granted a warrant exercisable for five (5) years to purchase 250 shares of common stock at $43.60 per share. The warrant expires on August 24, 2014. For financial reporting purposes, the Company recorded a debt discount expense of $10,000 to reflect the value of the warrants issued.

The Company made the payments due on September 30, 2008 and December 31, 2008, leaving a principal balance due of $2,044,000 due at December 31, 2008. The balance owed at December 31, 2009 amounted to $2,044,000.

Our obligation under both the Old Note and New Note are subordinate to our indebtedness to PNC and SCCF. In March 2009, the Company received a notice from SCCF, exercising their right to block payments under the New Note. Accordingly, the payment due on March 31 was not made. In April 2009, the Company received a notice from the holders of the New Note that an event of default had occurred, and accordingly, interest under the New Note would now accrue at 11% per annum. Per the terms of the fourth amendment to the SCCF Loan, all payments have been blocked until April 30, 2010. As a result of this, the Company has entered into a modification agreement with the holder of the New Note to amend the payment terms. The Company has paid a fee to the holder of $50,000 to modify the loan agreement to block the payments until April 30, 2010 and accrue interest at a rate of 9% per annum.

As of December 31, 2009, the aggregate future minimum payments for Notes Payable – Sellers are as follows:

Year	Amount
2010	$ 688,000
2011	348,000
2012	321,000
2013	344,000
2014	583,000
Sellers Notes Payable	2,284,000
Less: Current portion	688,000
Long-term portion	$ 1,596,000

Interest expense on these notes amounted to approximately $211,000 and $128,000 for the years ended December 31, 2009 and 2008, respectively. Amortization of debt accretion for the years ended December 31, 2009 and 2008 amounted to $0 and $93,000, respectively.

On September 30, 2010, the Company entered into letter agreement with the former stockholders of Welding Metallurgy. It was agreed that all interest that had been accrued and not yet paid would be capitalized into the principal balance of the note, making the new balance of the note $2,397,967. Payments on the note began on October 1, 2010. It was further agreed that payments would be made according to the following schedule: equal monthly installments of $40,000 on the first business day of each month until December 31, 2011, followed by equal monthly installments of $60,000 on the first business day of each month commencing on January 1, 2012 and continuing until the entire obligation is paid in full, which is estimated to be in January 2015. Interest shall accrue at the rate of 7% per annum, and each payment will first apply to interest and then principal.

As of October 1, 2010 the future minimum payments for the note payable to the former shareholders of Welding Metallurgy is as follows:

Year	Amount
2010	$ 93,000
2011	329,000
2012	601,000
2013	644,000
2014	690,000
2015	41,000
Former WMI Shareholder Notes Payable	2,398,000
Less: Current portion	93,000
Long-term portion	$ 2,305,000

Junior Subordinated Notes

In June 2008, we sold in a private placement to accredited investors, $2,950,000 principal amount of our junior subordinated notes (the "Old Notes"), together with 983,324 shares of our common stock, for total cash consideration of $2,950,000. The Old Notes bore interest at rates ranging up to 36% per annum and were originally payable on May 31, 2010, or earlier upon completion of one or a series of financings resulting in aggregate gross proceeds of at least $10 million. For financial reporting purposes, the Company recorded a discount of $195,000 to reflect the value of the common stock issued.

In September 2008 and October 2008, we sold in a private placement to accredited investors an additional $2,595,000 principal amount of junior subordinated notes, (the "New Notes") together with 207,600 shares of our Series B Preferred, for a total purchase price of $2,595,000. The New Notes, which were originally payable on May 31, 2010, or earlier upon completion of one or a series of financings resulting in aggregate gross proceeds of at least $10 million, bear interest at the rate of 1% per month (or 12% per annum). For financial reporting purposes, the Company recorded a discount of $1,396,000 to reflect the value of the Series B Preferred issued.

The terms of the New Notes and the Old Notes are identical, except that the rate of interest on the Old Notes was adjusted to 1% per month (12% per year) upon the issuance of the New Notes.

In October 2008, holders of the Old Notes exchanged their Old Notes for an equal principal amount of New Notes and also received 236,000 shares of Series B Preferred. For financial reporting purposes, the Company recorded a discount of $1,584,000 to reflect the value of the Series B Preferred issued.

In the first quarter ended March 31, 2009, we sold in a private placement to accredited investors, an additional $445,000 principal amount of New Notes together with 35,600 shares of our Series B Preferred for a total purchase price of $445,000. For financial reporting purposes, the Company recorded a discount of $239,000 to reflect the value of the Series B Preferred issued.

The New Notes are subordinated to the Company's senior indebtedness.

In connection with the offering of the Company's junior subordinated notes and Series B Preferred which commenced in September 2008 (see Note 10 Stockholders' Equity), the Company issued to Taglich Brothers, Inc. ("Taglich"), as placement agent, a junior subordinated note in the principal amount of $510,000 and 39,640 shares of Series B Preferred, The terms of the note issued to Taglich are identical to the New Notes. In addition, the Company issued a warrant to purchase 137,138 shares of its Series B Preferred to Taglich (see Note 10 Stockholders' Equity). For financial reporting purposes, the Company recorded a discount of $1,306,000 to reflect the commission, the value of the warrants issued and the value of the Series B Preferred issued. In connection with the amounts raised in 2009, the Company issued

Taglich 3,560 shares of Preferred Series B and will issue to Taglich a note on the same terms as the junior subordinated note referred to above for commission of $44,500. For financial reporting purposes, the Company recorded a discount of $68,000 to reflect the commission, the value of the warrants issued and the value of the Series B Preferred issued.

Amortization of debt discount amounted to $2,990,000 and $475,000 for the years ended December 31, 2009 and 2008 respectively. Interest expense amounted to $780,000 and $331,000 for the years ended December 31, 2009 and 2008, respectively.

In May 2010, the maturity dates of the New Notes were extended by the holders to September 30, 2010. On October 1, 2010, a payment in the amount of $50,000 was made to one of the note holders in full satisfaction of a note. During November 2010, the maturity dates of the New Notes were extended to November 18, 2013.

Note 10. STOCKHOLDERS' EQUITY

Authorized Shares

At a Special Meeting of Stockholders on April 3, 2008, the stockholders approved an amendment to the certificate of incorporation increasing to 250,000,000 the number of shares of Common Stock the Company is authorized to issue.

At a Special Meeting of Stockholders on July 29, 2010, the stockholders approved an amendment to the certificate of incorporation to effect a one-for four hundred (1-for-400) reverse split of our common stock, conversion of our Series B Convertible Stock into 3,400,000 shares of common stock and reduce the number of authorized shares of common stock from 250,000,000 to 20,000,000.

Common Stock Issuances

Issuances of Common Stock for the years ended December 31, 2009 and 2008 are as follows:

In June 2008, we sold in a private placement to accredited investors, $2,950,000 principal amount of our Old Notes together with 2,458 shares of our common stock. In addition, the Company issued to Taglich as placement agent, 500 shares of Common Stock as a partial sales commission. See Note 9 Notes Payable and Capital Lease Obligations.

During the three months ended March 31, 2008, the Company issued 350 shares of Common Stock to key employees under the 2005 Stock Incentive Plan. The Company incurred compensation expenses valued at $34,000.

During the year ended December 31, 2008, the Company issued 687 shares of Common Stock for services valued at $50,943.

In the third quarter of 2008, holders of 23,091 shares of Series B Preferred converted their shares and received 2,010 shares of Common Stock.

In June 2009, the Company issued 434 shares of Common Stock valued at $43,423 to two vendors of Sigma as per settlement agreements signed with each. See Note 12 Commitments and Contingencies.

On July 29, 2010 at a Special Meeting of Stockholders, the stockholders approved an amendment to the certificate of designation for the Series B Preferred Stock providing for the automatic conversion of the outstanding shares of Series B Preferred Stock, together with any dividends that are or may become payable prior to the conversion date, into 3,400,000 shares of Common Stock.

Series B Convertible Preferred Stock

By resolution, the Board of Directors of the Corporation has established, designated and fixed the terms, preferences, limitations and relative rights of two million (2,000,000) shares of the authorized and unissued preferred stock of the Corporation as Series B Preferred. Rights include the following:

1. Holders of the shares of Series B Preferred are entitled to receive 7% cumulative dividend of the original Series B Preferred issue price.
2. Dividends shall accrue and be payable quarterly on January 2, April 1, July 1 and October 1 of each year.
3. The Company can elect to deliver additional shares of Series B Preferred in lieu of cash payments.
4. The liquidation value is an amount equal to the greater of $10 per share or such amount per share as would have been payable had each such share been converted into Common Stock immediately prior to a liquidation event (as defined).
5. Each holder of outstanding shares of Series B Preferred shall be entitled to the number of votes equal to the number of whole shares of Common Stock into which the shares of Series B Preferred held by such holder are then convertible, at each meeting of stockholders of the Corporation (or by written action of stockholders in lieu of meeting) with respect to all matters presented to the stockholders of the Corporation for their action or consideration. The holders of Series B Preferred will generally vote together with the holders of Common Stock as a single class.
6. Each share of Series B Preferred is convertible, at the option of the holder thereof, at any time and from time to time, and without the payment of additional consideration by the holder thereof, into such number of fully paid and no assessable shares of Common Stock as is determined by dividing (i) the Series B Original Issue Price ($10) by (ii) the Series B Conversion Price (as defined) in effect at the time of conversion.

Issuances and conversions of Series B Preferred for the years ended December 31, 2009 and 2008 are as follows:

For the years ended December 31, 2009 and 2008, the Company issued 1,127,838 and 98,688 shares of Series B Preferred as dividends in lieu of cash payments, respectively. Dividends amounted to $1,455,000 and $620,000 for the years ended December 31, 2009 and 2008, respectively.

During 2008, the Company issued 206,800 shares of Series B Preferred to note holders in connection with the Company's placement of junior subordinated notes in September 2008. In addition, the Company issued to Taglich 39,640 shares of Series B Preferred as a partial sales commission. See Note 9 Notes Payable and Capital Lease Obligations.

In October 2008, holders of an aggregate of $2,950,000 of outstanding Old Notes issued in May and June 2008 exchanged their Old Notes for an equal principal amount of New Notes. In addition, the note holders received 236,000 shares of Series B Preferred.

In the third quarter of 2008, holders of 23,091 shares of Series B Preferred converted their shares and received 803,962 shares of Common Stock.

As of December 31, 2008, there were outstanding 1,387,205 shares of Series B Preferred. The shares of Series B Preferred outstanding at December 31, 2008 are convertible into 126,064 shares of common stock.

In January 2009, as part of the sale of certain of Sigma's assets to its former stockholders, such stockholders and the Company consummated a Settlement Agreement in which these notes were converted into 58,500 shares of Series B Preferred. See Note 9 Notes Payable and Capital Lease Obligations.

The Company issued 36,400 shares of Series B Preferred to note holders in connection with the Company's placement of junior subordinated notes in the first quarter of 2009. In addition, the Company issued to Taglich 3,560 shares of Series B Preferred as a partial sales commission.

In March 2009, the Company issued 4,211 shares of Series B Preferred valued at $25,000 to a vendor for services rendered in 2008.

In June 2009, the Company issued 10,000 shares of the Series B Preferred to Blair-HSM Companies in accordance with the settlement agreement, See Note 12 Commitments and Contingencies.

As of December 31, 2009, there were outstanding 2,627,714 shares of Series B Preferred which are convertible into 238,796 shares of common stock.

In January 2010, the Company issued 839,108 shares of Series B Preferred as dividends for the quarter ended December 31, 2009 in lieu of cash payments.

On January 5, 2010, the Company issued 137,138 shares of Series B Preferred for the exercise of 137,138 warrants. See Note 14 Stock Options and Warrants.

In April 2010, the Company issued 1,004,926 shares of Series B Preferred as dividends for the quarter ended March 31, 2010.

On July 29, 2010 at a Special Meeting of Stockholders, the stockholders approved an amendment to the certificate of designation for the Series B Preferred Stock providing for the automatic conversion of the outstanding shares of Series B Preferred Stock, together with any dividends that are or may become payable prior to the conversion date, into 3,400,000 shares of Common Stock. This represents 95% of the outstanding shares of Common Stock after giving effect to the reverse stock split.

Note 11. EMPLOYEE BENEFITS PLANS

The Company employs both union and non-union employees and maintains several benefit plans.

For the period January 2008 through August 2008, the Union provided medical benefit plans at defined rates which were contributed in their entirety by the Company. Beginning in September 2008 and continuing through 2009, medical benefits were provided through a policy with Administaff, the costs of which are borne by the Company. In addition, the Company is obligated to contribute to a welfare fund and a security fund for the benefit of each union employee of between $50 and $250 per month.

All other Company employees including those of Welding are covered under a co-employment agreement with Administaff.

The Company has two defined contribution plans under Section 401(k) of the Internal Revenue Code (the "Plans"). Pursuant to the Plans, qualified employees may contribute a percentage of their pretax eligible compensation to the Plan. The Company does not match any contributions that employees may make to either Plan.

Note 12. COMMITMENTS AND CONTINGENCIES

Real Estate Leases

The Company leases its facilities under various operating lease agreements, which contain renewal options and escalation provisions. Rent expense was $1,210,000 and $1,109,000 for the years ended December 31, 2009 and 2008, respectively. The Company is responsible for paying all operating costs under the term of the lease. As of December 31, 2009, the aggregate future minimum lease payments are as follows:

Year	Plant Avenue Annual Rent	Fifth Avenue Annual Rent	Total Rents
2010	$ 546,000	$ 540,000	$ 1,086,000
2011	562,000	560,000	1,122,000
2012	579,000	626,000	1,205,000
2013	597,000	644,000	1,241,000
2014	614,000	663,000	1,277,000
thereafter	633,000	9,462,000	10,095,000
Total Rents	$ 3,531,000	$ 12,495,000	$ 16,026,000

The lease provides for scheduled increases in base rent. Rent expense is charged to operations using the straight-line method over the term of the lease which results in rent expense being charged to operations at inception of the lease in excess of required lease payments. This excess is shown as deferred rent in the accompanying balance sheet.

Sigma was located in the Plant Avenue facility and following discontinuing operations, a portion of the facility is vacant. The Company has been seeking a sub-tenant to rent the space but has been unsuccessful. The Company recorded a charge for $579,000 at December 31, 2009 representing the estimated discounted future cost of part of the Plant Avenue facility.

As of December 31, 2009, the estimated expected future cost will be repaid as follows:

Year	Amount
2010	$ 223,000
2011	96,000
2012	85,000
2013	72,000
2014	59,000
2015	44,000
Total future minimum lease payments	579,000
Less: current portion	(223,000)
Total Long-Term Portion	$ 356,000

On July 1, 2010, the Company entered into a sub-lease with a third party to rent a portion of the vacant space at the Plant Avenue facility. Under the terms of the sub-lease, the sub-tenant would occupy approximately 17,787 square feet for the months of July 2010 through October 2010. Beginning in November 2010, the sub-tenant would occupy approximately 27,787 square feet. The space is being sub-leased for $3.00 per square foot, with a discount in the first month of 50%. The sub-lease is a month-to-month lease and can be terminated by either party with 90 days written notice.

Litigation

Blair – HSM Companies: During the first half of 2008, and continuing into the third quarter of 2008, the Company attempted to acquire Blair Industries, Inc. and certain of its affiliated companies ("Blair-HSM"). During the third quarter of 2008, management determined to cease its efforts to acquire Blair-HSM. On November 3, 2008, we were served with an Information Request and Restraining Notice by the Blair-HSM as part of their efforts to collect on the $350,000 Confession of Judgment issued by us to secure our agreement to reimburse the stockholders of Blair-HSM for certain expenses incurred in connection with the acquisition.

On November 28, 2008, we entered into a settlement agreement with the former stockholders of Blair-HSM under which we agreed to pay Blair-HSM $350,000 in full and complete satisfaction of amounts payable under the stock purchase agreement as follows: $250,000 in cash payments in 2009 with the balance payable by delivery of 10,000 shares of our Series B Preferred having a face value of $100,000. Such amount was accrued and included as part of Accounts Payable and Accrued Expenses as of December 31, 2008 The payments were made in 2009 and the shares were issued in June 2009.

In connection with the settlement, the former shareholders of Blair-HSM and Blair-HSM agreed to file a Satisfaction of Judgment with the Supreme Court of the State of New York, Suffolk County.

Sigma Metals, Inc: Several former vendors to Sigma have commenced legal action against Sigma seeking to recover amounts owed to them. While Sigma has no significant assets remaining, we have been attempting to negotiate settlements of these claims. One former vendor has been awarded a judgment against Sigma in the amount of approximately $107,000. This matter has been resolved and a satisfaction of judgment has been received. Another, former vendor commenced litigation in 2009 and in January 2010, this litigation was settled for approximately $100,000 payable in installments over approximately six (6) months. During 2009, the Company signed settlement agreements with vendors for payables by issuing 434 shares of common stock valued at $43,423. See Note 10 Stockholders' Equity. Several other vendors have been awarded judgments and/or are deciding to commence litigation subsequent to December 31, 2009. All of these claims have been settled and released. The total amount sought by these vendors was approximately $778,000, and was settled for approximately $245,000. One additional vendor is deciding to commence litigation seeking the recovery of approximately $71,000. Settlement discussions have commenced with this vendor but there is not yet a definitive resolution.

Employment Contracts

In September 2005, the Company entered into employment agreements (the "Agreements") with four senior executives that became effective November 30, 2005. The Agreements are for an initial period of five years until September 2010 and, absent notice of non-renewal given ninety (90) days prior thereto, are automatically extended for successive three (3) one year periods unless terminated. The Board, at its sole discretion, determines whether a bonus is issued, provided that in the case of two executives, the amount of the bonus shall be predicated on their performance and the achievement by the Company of its operating targets set forth in its annual budget, and in the case of these two executives, provided further, in no event shall the amount of their bonuses be less than 50% of their salary at that time. For the years ended December 31, 2009 and 2008 no bonuses were paid. Each senior executive's agreement also call for grants of stock options to purchase the Company's common stock aggregating 12,125 shares of which 8,525 had been granted as of December 31, 2007. No additional stock options were granted during 2008 or 2009.

The Company and one of its four senior executives mentioned above entered into a Separation Agreement and General Release (the "Separation Agreement") effective March 16, 2007. In lieu of the compensation payable to the executive pursuant to his Employment Agreement, from March 16, 2007 to November 30, 2010, the executive will be paid at a rate of $100,000 per annum and from December 1, 2010 to May 31, 2011; he will be paid at a rate of $50,000 per annum. In addition, if the Company achieves certain agreed-upon levels of performance, he may receive up to an additional $50,000. The remaining amounts owed to the executive totaling $116,655 have been accrued and included in Accounts Payable and Accrued Expenses at December 31, 2009. Upon the execution of his employment agreement mentioned above, the Company granted this executive, options to purchase 3,125 shares of Common Stock, subject to an agreed upon vesting schedule and exercisable over a ten-year period commencing on the date of grant. Pursuant to the Separation Agreement, all unvested options held by this executive vested as of March 16, 2007, and the right to exercise all of his options terminated as of March 16, 2008.

In April 2007, the Company entered into employment agreements (the "Sigma Agreements") with the former stockholders of Sigma. The Sigma Agreements were for a period of five years. In January 2009, as part of the sale of Sigma to its former stockholders, such stockholders and the Company consummated a Settlement Agreement in which the Sigma Agreements were terminated.

Note 13. INCOME TAXES

The provision for income tax benefits at December 31, 2009 and 2008 consists of the following:

	2009	2008 (Restated)
Current		
Federal	$ (317,000)	$ -
State	(17,000)	1,000
Total Current (Benefit) Provision	(334,000)	1,000
Deferred		
Federal	(1,093,000)	(715,000)
State	(272,000)	(30,000)
Total Deferred Taxes	(1,365,000)	(745,000)
Net (Benefit) Provision for Income Taxes	$ (1,699,000)	$ (744,000)

The total current income tax benefits for the year ended December 31, 2009 represent federal and state refunds received from net operating loss carrybacks.

The components of net deferred tax liabilities as of December 31, are set forth below:

Deferred tax assets:	2009	2008 (Restated)
Net operating loss carry forwards	$ 1,072,000	$ 936,000
Bad debts	156,000	72,000
Inventory - 263A adjustment	-	403,000
Stock based compensation - warrants	-	44,000
Stock based compensation - options and restricted stock	266,000	327,000
Goodwill and Intangibles	1,644,000	-
Account payable, accrued expenses and reserves	206,000	1,219,000
Deferred rent	244,000	147,000
Deferred gain on sale of real estate	255,000	237,000
Total deferred tax assets before valuation allowance	3,843,000	3,385,000
Valuation allowance	(1,615,000)	(3,110,000)
Total deferred tax assets after valuation allowance	2,228,000	275,000
Deferred tax liabilities:		
Property and equipment	(950,000)	(530,000)
Capitalized engineering costs	(501,000)	(289,000)
Amortization - Welding Transaction	(777,000)	(820,000)
Total Deferred Tax Liability	(2,228,000)	(1,639,000)
Net deferred tax liability	$ -	$ (1,364,000)

Realization of deferred tax assets is dependent on future earnings. Due to the uncertainty of realization of the net deferred tax assets, the Company has provided a valuation allowance. In assessing the realizability of it, management considers whether it is more likely than not that some or perhaps all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making the assessment. The valuation allowance at December 31, 2009 and 2008 amounted to $1,750,000 and $3,110,000, respectively.

The Company has net operating losses totaling $2,679,000 which will expire in fiscal 2028 and 2029.

At December 31, 2009 and 2008, the Company had no material unrecognized tax benefits and no adjustments to liabilities or operations were required. The Company does not expect that its unrecognized tax benefits will materially increase within the next twelve months. We recognize interest and penalties related to uncertain tax positions in general and administrative expense. As of December 31, 2009 and 2008, we have not recorded any provisions for accrued interest and penalties related to uncertain tax positions.

In certain cases, the Company's uncertain tax positions are related to tax years that remain subject to examination by the relevant tax authorities. The Company files U.S. and state income tax returns in jurisdictions with varying statutes of limitations. The 2006 through 2008 tax years generally remain subject to examination by federal and state tax authorities.

Note 14. STOCK OPTIONS AND WARRANTS

Stock-Based Compensation

During 2005, the Company's Board of Directors approved a stock option plan and reserved 25,000 shares of its Common Stock for issuance under the plan. The stock option plan permits the Company to grant non-qualified and incentive stock options to employees, directors, and consultants. There were no awards granted during 2009. Awards granted during 2008 under the Company's plans vest over zero, one and five years. The weighted average fair values of options granted during the year end December 31, 2008 was $88.00. The fair value of each option grant was estimated on the date of grant using the Black Scholes option pricing model using weighted average assumptions for grants as follows:

Expected life of option	3-5.5 years
Risk-free interest rates	2.60%
Volatility of stock	133%
Expected dividend yields	0%

The expected life is the number of years that the Company estimates, based upon history, that options will be outstanding prior to exercise or forfeiture. In addition to the inputs referenced above regarding the option pricing model, the Company adjusts the stock-based compensation expense for estimated forfeiture rates that are revised prospectively according to forfeiture experience.

Certain of the Company's stock options contain features which include variability in grant prices. A portion of the currently issued stock options will be priced based on average trading prices of the Company's Common Stock at the end of a given future period. Due to this variable feature, these stock options are not deemed to be granted for purposes of applying FASB ASC 718 and accordingly, their fair value will be calculated and expensed in future periods.

On February 13, 2007, we issued to each of the non-management members of the Board, an option to purchase 250 shares of our common stock. The options vested as to 83 shares upon grant, as to a total of 166 on March 1, 2008 and will vest as to all 250 shares on March 1, 2009. The options are exercisable at a price of $108.00 per share until March 1, 2014.

On August 29, 2007, we granted David Buonanno, a non-management director, an option to purchase 250 shares of our common stock, which was immediately exercisable as to 83 shares. The option will become exercisable as to a total of 166 shares on June 26, 2008, and as to all 250 shares on June 26, 2009. The exercise price of the option is $112.00 per share. The option expires on August 1, 2014.

On April 11, 2008, we granted each non-management director an option to purchase 250 shares of common stock at an exercise price per share of $90.00 exercisable immediately for five years. In addition, the terms of the options previously granted to Messrs. Rettaliata, Giusto and Peragallo were modified to provide that the options scheduled to vest from 2008 through 2012, 3,600 options in the aggregate, The exercise price of the options vesting on each of September 15, 2009, 2010, 2011 and 2012 will be (a) $88.00 per share or (b) the average trading price of our common stock for the thirty trading days ending September 15, 2008, 2009, 2010, 2011 and September 15, 2012, respectively.

The Company recorded expenses of $102,000 and $203,000 in its consolidated statement of operations for the years ended December 31, 2009 and 2008, respectively, and is included as a component of general and administrative expense.

A summary of the status of the Company's stock options as of December 31, 2009, and changes during the two years then ended is presented below.

	Options	Wtd. Avg. Exercise Price
Balance, December 31, 2007	18,543	$ 124.00
Granted during the period	1,075	92.00
Exercised during the period	-	-
Terminated/Expired during the period	(3,311)	96.00
Balance, December 31, 2008	16,307	120.00
Granted during the period	-	-
Exercised during the period	-	-
Terminated/Expired during the period	(377)	104.00
Balance, December 31, 2009	15,930	$ 120.00
Exercisable	11,014	$ 136.00

The following table summarizes information about stock options at December 31, 2009:

Range of Exercise Prices	Remaining Number Outstanding	Wtd. Avg. Life	Wtd. Avg. Exercise Price
$ 88 - 116	11,980	3 years	$ 100.00
$ 117 - 168	1,975	4 years	$ 172.00
$ 169 - 192	1,975	4 years	$ 192.00
	15,930	4 years	$ 120.00

As of December 31, 2009, there was $537,000 of unrecognized compensation cost related to non-vested stock option awards, which is to be recognized over the remaining weighted average vesting period of five years.

The aggregate intrinsic value at December 31, 2009 was $0. The aggregate intrinsic value was calculated based on the positive difference between the closing market price of the Company's Common Stock and the exercise price of the underlying options.

At a Special Meeting of Stockholders held on July 29, 2010, the stockholders approved the 2010 Equity Incentive Plan and the issuance of 284,437 options under the plan to various key employees of the Company. This plan had previously been unanimously adopted by the Board of Directors.

Warrants

The Company issued warrants for the following transactions:

On December 31, 2008, the Company issued a warrant to purchase 137,138 shares of its Series B Preferred Taglich for nominal consideration. The warrant was issued to compensate Taglich for its continued efforts to raise funds on behalf of the Company. The warrant may be exercised until December

31, 2015. The exercise price of the warrant is $0.01 per share. On January 5, 2010, the warrant was exercised. See Note 10 Stockholders' Equity.

In connection with the acquisition of Welding, the Company incurred a note payable to the former stockholders of Welding. In August 2008, the Company and the former stockholders reached an agreement restructuring the Company's obligation under this note. As additional consideration, the former stockholders were granted a warrant exercisable for five (5) years to purchase 250 shares of common stock at $43.60 per share. The warrant expires on August 24, 2014. See Note 9 Notes Payable and Capital Lease Obligations.

The following tables summarize the Company's outstanding warrants as of December 31, 2009 and changes during the two years then ended:

	Warrants	**Wtd. Avg. Exercise Price**
Balance, December 31, 2007	19,615	$ 100.00
Granted during the period	593	84.00
Exercised during the period	-	-
Terminated/Expired during the period	-	-
Balance, December 31, 2008	20,208	100.00
Granted during the period	-	-
Exercised during the period	-	-
Terminated/Expired during the period	-	-
Balance, December 31, 2009	20,208	$ 100.00
Exercisable	20,208	$ 100.00

The following table summarizes information about warrants at December 31, 2009:

Range of Exercise Prices	**Warrants**	**Wtd. Avg. Life**	**Wtd. Avg. Exercise Price**
$ 0.00 - 84	1,955	2 years	$ 72.00
$ 85 - 116	11,002	2 years	$ 88.00
$ 117 - 168	7,251	2 years	$ 124.00
	20,208	2 years	$ 100.00

Note 15. RELATED PARTY TRANSACTIONS

On December 31, 2008, the Company issued a warrant to purchase 137,138 shares of its Series B Preferred to Taglich for nominal consideration. The Company believes that the terms of the warrant are not less favorable than could have been obtained from an unaffiliated third party. On January 5, 2010, Taglich exercised this warrant and were issued 137,138 shares of Series B Preferred. See Note 14 Stock Options and Warrants.

In connection with the offering of the Company's junior subordinated notes and Series B Preferred which commenced in September 2008, the Company issued to Taglich a junior subordinated note in the principal amount of $510,000 and 39,640 shares of Series B Preferred. In connection with the amounts raised in 2009, the Company issued Taglich 3,560 shares of Preferred Series B and will pay Taglich a commission of $44,500. See Note 8 Notes Payable and Capital Lease Obligation. In addition, the Company granted Taglich the right to designate a total of three nominees for election to our Board of Directors, which nominees are Michael N. Taglich, Robert F. Taglich and Robert Schroeder. Michael N. Taglich, Chairman of the Company's Board of Directors, is President and Chairman of Taglich, Robert F. Taglich is a Managing Director of, and Robert Schroeder is Vice President - Investment Banking of, Taglich.

Taglich acted as placement agent for the sale of our junior subordinated notes in June 2008. For acting as placement agent of our junior subordinated notes in May and June 2008, we paid Taglich a fee of $20,000 in cash plus 200,000 shares of our Common Stock, as well as reimbursement of approximately $25,000 of out-of-pocket expenses. See Note 9 Notes Payable and Capital Lease Obligations.

Note 16. DISCONTINUED OPERATIONS

During the quarter ended September 30, 2008, the Company's Board of Directors decided to discontinue the operations at Sigma. Operations were discontinued on October 31, 2008. Accordingly, Sigma's results of operations have been reported as discontinued operations for all periods presented. Sigma's assets and liabilities have been classified as held for sale on the Company's consolidated balance sheet for all periods presented.

	2009	2008 (Restated)
Net Sales	$ 210,000	$10,206,000
Cost of Sales	990,000	10,555,000
Gross loss	(780,000)	(349,000)
Operating costs and expenses	478,000	3,791,000
Loss from operations	(1,258,000)	(4,140,000)
Interest and financing costs	28,000	57,000
Recovery of Bad Debt	638,000	-
Debt Forgivness Income	224,000	-
Write-off of Goodwill	-	1,550,000
Write-off of Intangibles	-	3,329,000
Net Loss	$ (424,000)	$(9,076,000)

Note 17. SEGMENT REPORTING

In accordance with FASB ASC 280, "Segment Reporting", the Company discloses financial and descriptive information about its reportable operating segments. Operating segments are components of an enterprise about which separate financial information is available and regularly evaluated by the chief operating decision maker in deciding how to allocate resources and in assessing performance.

As a result of the acquisition of Welding in August 2007, the Company is operating in two segments. As discussed above, Sigma, which was acquired in April 2007, was discontinued in October 2008. Financial information about the Company's operating segments for the years ended December 31, 2009 and 2008 is as follows:

Year Ended December 31,	2009	2008 (Restated)
Air Industries Machining		
Net Sales	$ 39,354,000	$ 34,746,000
Gross Profit	6,347,000	6,586,000
Pre Tax Income	1,627,000	556,000
Assets	29,577,000	31,523,000
Sigma Metals		
Loss From Discontinued Operations	(424,000)	(9,076,000)
Assets Held for Sale	1,127,000	1,124,000
Welding Metallurgy		
Net Sales	5,497,000	3,948,000
Gross Profit	1,801,000	2,144,000
Pre Tax Income (Loss)	327,000	(2,776,000)
Assets	6,475,000	5,773,000
Corporate		
Net Sales	-	-
Gross Profit	-	-
Pre Tax Loss	(6,287,000)	(6,322,000)
Assets	12,050,000	14,953,000
Consolidated		
Net Sales	44,851,000	38,694,000
Gross Profit	8,148,000	8,730,000
Loss from Discontinued Operations	(424,000)	(9,076,000)
Pre Tax Loss	(4,333,000)	(8,542,000)
Benefit for Taxes	(1,699,000)	(744,000)
Net Loss	(3,058,000)	(16,874,000)
Elimination of Assets	(11,752,000)	(12,945,000)
Assets	37,477,000	40,428,000