

**Not filed with the Securities and Exchange Commission. Furnished pursuant to the indentures governing the 8.5% Senior Fixed Rate Notes due 2015, 8.875%/9.625% Senior PIK-Election Notes due 2015 and 9.75% Senior Subordinated Notes due 2017 of Hawker Beechcraft Acquisition Company LLC and Hawker Beechcraft Notes Company and the \$1,810 million Senior Secured Credit Facility of Hawker Beechcraft Acquisition Company LLC and Hawker Beechcraft Notes Company.**

**SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549**

**Form 10-Q**

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the Quarter Ended March 25, 2007**

or

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**Hawker Beechcraft Acquisition Company LLC  
Hawker Beechcraft Notes Company**  
(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**71-1018770  
20-8650498**  
(I.R.S. Employer  
Identification Number)

**10511 East Central  
Wichita, Kansas 67206  
(316) 676-7111**

(Address, including zip code, and telephone number, including  
area code, of registrant's principal executive offices)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

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**Raytheon Aircraft**  
**Condensed Consolidated Balance Sheets (Unaudited)**  
(In millions)

	(Unaudited) March 25, 2007	December 31, 2006
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$15.1	\$25.9
Accounts and notes receivable, net of allowance for doubtful accounts of \$1.5 at March 25, 2007 and \$1.2 at December 31, 2006	100.9	110.7
Finance receivables, net of allowance for doubtful accounts of \$0.6 at March 25, 2007 and \$0.8 at December 31, 2006	38.2	57.0
Unbilled revenue	60.5	27.4
Inventories	1,531.6	1,446.0
Current deferred income taxes	96.4	109.0
Prepaid expenses and other current assets	44.1	70.6
Total current assets	1,886.8	1,846.6
Property, plant, and equipment, net	530.6	520.8
Intangible assets, net	50.8	53.1
Long-term finance receivables	10.2	6.8
Other assets, net	106.6	111.2
Total assets	\$2,585.0	\$2,538.5
<b>Liabilities and Invested Equity</b>		
Current liabilities		
Advance payments and billings in excess of costs incurred	\$ 379.0	\$424.5
Accounts payable	354.9	360.5
Accrued salaries and wages	34.8	38.2
Other accrued expenses	218.1	227.6
Total current liabilities	986.8	1,050.8
Accrued retiree benefits and other long-term liabilities	169.4	165.5
Deferred income taxes	55.2	78.1
Total liabilities	1,211.4	1,294.4
Commitments and contingencies (Note 10)		
Accumulated other comprehensive loss	(83.5)	(85.9)
Parent company investment	1,457.1	1,330.0
Total invested equity	1,373.6	1,244.1
Total liabilities and invested equity	\$2,585.0	\$2,538.5

The accompanying notes are an integral part of these condensed consolidated financial statements.

**Raytheon Aircraft**  
**Condensed Consolidated Statements of Operations (Unaudited)**  
(In millions)

	Three Months Ended	
	March 25, 2007	March 26, 2006
Sales:		
Aircraft, parts and services	\$647.3	\$479.7
Sales to related parties	20.5	24.9
Total sales	<u>667.8</u>	<u>504.6</u>
Cost of sales:		
Aircraft, parts and services	545.6	406.7
Sales to related parties	20.5	24.8
Total cost of sales	<u>566.1</u>	<u>431.5</u>
Gross margin	<u>101.7</u>	<u>73.1</u>
Selling, general and administrative expenses	52.0	44.8
Research and development expenses	<u>21.3</u>	<u>18.2</u>
Operating income	<u>28.4</u>	<u>10.1</u>
Intercompany interest expense, net	15.8	20.1
External interest income, net	(0.9)	(4.6)
Other income, net	<u>(0.1)</u>	<u>(0.6)</u>
Non-operating expense, net	<u>14.8</u>	<u>14.9</u>
Income (loss) before taxes	13.6	(4.8)
Provision for (benefit from) income taxes	<u>5.1</u>	<u>(1.7)</u>
Net income (loss)	<u>\$8.5</u>	<u>\$(3.1)</u>

The accompanying notes are an integral part of these consolidated financial statements

**Raytheon Aircraft**  
**Condensed Consolidated Statements of Cash Flows (Unaudited)**  
(In millions)

	<b>Three Months Ended</b>	
	<b>March 25, 2007</b>	<b>March 26, 2006</b>
Cash flows from operating activities:		
Net income (loss)	<b>\$8.5</b>	\$(3.1)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	<b>21.9</b>	22.2
Deferred income taxes	<b>4.5</b>	(1.7)
Changes in assets and liabilities:		
Accounts receivable	<b>9.8</b>	(1.9)
Unbilled revenue, advance payments and billings in excess of costs incurred	<b>(78.6)</b>	116.4
Inventories	<b>(85.6)</b>	(157.1)
Prepaid expenses and other current assets	<b>26.5</b>	23.9
Accounts payable	<b>(5.6)</b>	32.5
Accrued salaries and wages	<b>(3.4)</b>	(15.3)
Other accrued expenses	<b>(9.5)</b>	(22.5)
Pension and other changes, net	<b>(6.2)</b>	8.3
Origination of financing receivables	<b>(20.6)</b>	(44.0)
Collection of financing receivables not sold	<b>36.2</b>	64.9
Net cash provided by (used in) operating activities	<b>(102.1)</b>	22.6
Cash flows from investing activities:		
Expenditures for property, plant, and equipment	<b>(26.2)</b>	(8.1)
Additions to intangible assets	<b>(1.1)</b>	(0.6)
Net cash used in investing activities	<b>(27.3)</b>	(8.7)
Cash flows from financing activities:		
Net transfers from (to) Raytheon	<b>118.6</b>	(17.7)
Change in notes payable and long-term debt	<b>-</b>	1.0
Net cash provided by (used in) financing activities	<b>118.6</b>	(16.7)
Net decrease in cash and cash equivalents	<b>(10.8)</b>	(2.8)
Cash and cash equivalents at beginning of year	<b>25.9</b>	25.7
Cash and cash equivalents at end of period	<b>\$15.1</b>	\$22.9

The accompanying notes are an integral part of these condensed consolidated financial statements.

# Raytheon Aircraft

## Notes to Condensed Consolidated Financial Statements

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### 1. Background and Basis of Presentation

Hawker Beechcraft, Inc. (“HBI”) was formed in late 2006 by GS Capital Partners VI, L.P., an affiliate of Goldman Sachs, and Onex Partners II LP, an affiliate of Onex Corporation, for the purpose of purchasing the Raytheon Aircraft business (“RA”) from Raytheon Company (“Raytheon”) (the “Acquisition”). On March 26, 2007, subsequent to the closing of RA’s fiscal quarter, the transaction was completed. HBI completed the Acquisition by acquiring all of the outstanding membership interests of Raytheon Aircraft Acquisition Company LLC (which was renamed Hawker Beechcraft Acquisition Company LLC “HBAC”) and substantially all of the assets of Raytheon Aircraft Services Limited. Following the Acquisition, HBI contributed the equity interest of the entity purchasing the assets of Raytheon Aircraft Services Limited to HBAC. RA is engaged in the design, development, manufacturing, marketing, selling and servicing of business and general aviation, training and special mission aircraft. HBAC and its subsidiaries together represent substantially all of the operations of RA.

These unaudited condensed consolidated financial statements have been prepared using the same basis as used by RA, the predecessor business, in the preparation of its 2006 audited consolidated financial statements and do not reflect the impact of the Acquisition. During the period covered by these unaudited condensed consolidated financial statements, RA was comprised of Raytheon Aircraft Holdings Inc., a wholly owned subsidiary of Raytheon, and substantially all of its subsidiaries as well as certain assets and liabilities of Raytheon. Excluded from RA was its investment in Flight Options LLC and Raytheon Aircraft Credit Corporation’s commuter operations and associated assets as those activities had separate cash flows and were operated and managed separately from RA.

These unaudited condensed consolidated financial statements have been derived from the accounting records of Raytheon using historical bases of assets and liabilities. HBI management believes the assumptions underlying the unaudited condensed consolidated financial statements are reasonable. However, the unaudited condensed consolidated financial statements included herein may not necessarily reflect HBAC’s results of operations, financial position and cash flows in the future or what its results of operations, financial position and cash flows would have been had HBAC operated as a stand-alone entity during the period presented. Certain adjustments to reflect assets and liabilities retained by Raytheon as part of the Acquisition are summarized in a pro forma basis in Note 2 below.

Certain information and footnote disclosures normally included in consolidated financial statements, prepared in accordance with generally accepted accounting principles in the United States of America (GAAP) have been condensed or omitted. The year-end condensed balance sheet data was derived from the audited financial statements of RA, but does not include all disclosures required by GAAP. In the opinion of HBAC management, these condensed consolidated financial statements reflect all adjustments, which are of a normal recurring nature, necessary for the presentation of financial statements for interim periods in accordance with GAAP and with the instructions to Form 10-Q in Article 10 of Regulation S-X.

**Raytheon Aircraft**  
**Notes to Condensed Consolidated Financial Statements**

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**2. Subsequent Event**

As noted above, HBI completed the Acquisition on March 26, 2007. In accordance with the purchase agreement, certain asset and liabilities of RA, as summarized below, were retained by Raytheon and will not become part of the HBAC business going forward.

**Assets and Liabilities Retained by Raytheon**

(In millions)

<u>Assets</u>	
Cash	<b>\$3.7</b>
Certain finance receivables	<b>6.6</b>
Investment in General Aviation Receivables Corp., a qualified special purpose entity under SFAS 140	<b>63.3</b>
Deferred tax asset	<b>96.4</b>
Miscellaneous retained assets	<b>1.2</b>
	<b>171.2</b>
<u>Liabilities</u>	
Product liability reserves	<b>\$26.8</b>
UK pension liabilities	<b>27.0</b>
Certain environmental reserves	<b>8.1</b>
Income and indirect tax liabilities	<b>125.3</b>
Other accrued liabilities	<b>2.9</b>
Miscellaneous retained liabilities	<b>3.9</b>
	<b>194.0</b>
Net liabilities retained by Raytheon	<b>\$22.8</b>

**3. Comprehensive Income**

Accumulated other comprehensive income or (loss) consisted of the following at:

<b>Accumulated Other Comprehensive Income or (Loss)</b> (In millions)	<b>March 25, 2007</b>	<b>December 31, 2006</b>
Unfunded projected benefit obligation	<b>\$(104.4)</b>	\$(109.9)
Foreign exchange translation	<b>(0.9)</b>	-
Cash flow hedges	<b>18.3</b>	20.2
Unrealized gains on investments	<b>3.5</b>	3.8
Total	<b>\$(83.5)</b>	\$(85.9)

The unfunded projected benefit obligation is shown net of tax benefits of \$56.2 million and \$59.2 million at March 25, 2007 and December 31, 2006, respectively. The cash flow hedges are shown net of tax liabilities of \$9.8 million and \$10.9 million at March 25, 2007 and December 31, 2006, respectively. Unrealized gains on investments are shown net of tax liabilities of \$1.9 million and \$2.0 million at March 25, 2007 and December 31, 2006, respectively.

**Raytheon Aircraft**  
**Notes to Condensed Consolidated Financial Statements**

The computation of comprehensive income was as follows:

<b>Comprehensive Income</b> (In millions)	<b>Three Months Ended</b>	
	<b>March 25, 2007</b>	<b>March 26, 2006</b>
Net income or (loss)	<b>\$8.5</b>	\$(3.1)
Amortization of minimum pension liability	-	0.1
Amortization of unfunded projected benefit obligation	<b>5.5</b>	-
Foreign currency translation adjustments	<b>(0.9)</b>	0.2
Unrealized gains (losses) on cash flow hedges	<b>(1.9)</b>	4.6
Unrealized losses on investments	<b>(0.3)</b>	(0.1)
<b>Total comprehensive income</b>	<b>\$10.9</b>	\$1.7

**4. Product Warranty**

Warranty provisions related to commercial aircraft and part sales are determined based upon an estimate of costs that may be incurred for warranty services over the period of coverage from 1 to 10 years. RA estimates its warranty costs based on historical warranty claim experience. The warranty accrual is reviewed quarterly to verify that it properly reflects the remaining obligation based on the anticipated expenditures over the balance of the obligation period. Adjustments are made when actual warranty claim experience differs from estimates. Activity related to commercial aircraft and part warranty provisions was as follows:

(In millions)	
Balance at December 31, 2006	<b>\$57.5</b>
Accruals for aircraft and part deliveries in Q1 2007	<b>8.1</b>
Accruals (reversals) related to prior year aircraft and part deliveries	<b>(0.1)</b>
Warranty services provided in Q1 2007	<b>(4.2)</b>
<b>Balance at March 25, 2007</b>	<b>\$61.3</b>

Warranty provisions related to aircraft sales performed under long-term contracts are accounted for as contract costs as the work is performed. The estimation of these costs is an integral part of the accounting for long-term contracts.

**5. Inventories**

Inventories consisted of the following at:

(In millions)	<b>March 25, 2007</b>	December 31, 2006
Finished goods	<b>\$349.0</b>	\$334.7
Work in process	<b>918.6</b>	852.6
Materials and purchase parts	<b>264.0</b>	258.7
<b>Total</b>	<b>\$1,531.6</b>	\$1,446.0

**Raytheon Aircraft**  
**Notes to Condensed Consolidated Financial Statements**

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**Lot Accounting**

RA uses lot accounting for new commercial aircraft introductions. Lot accounting involves selecting a lot size at the time a new aircraft begins to be delivered and measuring an average margin over the entire lot for each aircraft sold. The costs attributed to aircraft delivered are based on the estimated average margin of all aircraft in the lot and are determined under the learning curve concept, which anticipates a predictable decrease in unit costs from cost reduction initiatives and as tasks and production techniques become more efficient through repetition. The size of the lot for the Beechcraft Premier is 200 units of which 181 had been delivered at March 25, 2007. There were 13 units for the Beechcraft Premier in backlog, of which 5 units are expected to be delivered from the lot. The size of the lot for the Hawker 4000 is 75 units, and no units had been delivered at March 25, 2007. There were 77 units for the Hawker 4000 in backlog, of which 38 units are expected to be delivered from the lot. Costs incurred on in process and delivered aircraft in excess of the estimated average margin were included in the work in process inventories and totaled \$0.9 million for the Beechcraft Premier and \$145.7 million for the Hawker 4000 as of March 25, 2007.

**6. Property, Plant, and Equipment**

Property, plant, and equipment consisted of the following at:

(In millions)	<b>March 25, 2007</b>	December 31, 2006
Land	<b>\$4.7</b>	\$4.7
Buildings and leasehold improvements	<b>192.4</b>	192.4
Aircraft and autos	<b>113.2</b>	110.8
Furniture, fixtures and office equipment	<b>20.9</b>	20.9
Tooling	<b>615.0</b>	607.6
Machinery and equipment	<b>289.3</b>	290.0
Construction in process	<b>37.2</b>	18.8
	<b>1,272.7</b>	1,245.2
Less accumulated depreciation	<b>742.1</b>	724.4
Total	<b>\$530.6</b>	\$520.8

Depreciation expense was \$18.7 million and \$19.0 million for the quarters ended March 25, 2007 and March 26, 2006, respectively.

**Raytheon Aircraft**  
**Notes to Condensed Consolidated Financial Statements**

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**7. Intangible Assets**

Intangible assets consisted of the following at:

(In millions)	March 25, 2007	December 31, 2006
Computer Software	\$90.6	\$89.7
Production Drawings	14.8	14.8
Intellectual Property Rights	21.2	21.2
	<b>126.6</b>	<b>125.7</b>
Less accumulated amortization	75.8	72.6
Total	<b>\$50.8</b>	<b>\$53.1</b>

Amortization expense was \$3.2 million for the quarters ended March 25, 2007 and March 26, 2006, respectively.

**8. Income Taxes**

RA's operating results have historically been included in Raytheon's consolidated U.S. federal tax return. The provision for income taxes in these financial statements has been determined on a separate return basis. Under this method, RA is assumed to file a separate return from Raytheon; reporting its taxable income or loss and paying applicable tax based on its separate taxable income and associated tax attributes.

On January 1, 2007, RA adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes ("FIN 48"), which clarifies the accounting for uncertainty in income tax positions. This interpretation requires the recognition in the consolidated financial statements of only those tax positions determined to be more likely than not of being sustained upon examination, based on the technical merits of the positions. FIN 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The cumulative effect of applying this interpretation was recorded as a decrease of \$2.9 million in retained earnings (a component of parent company investment in these financial statements), an increase of \$16.0 million in net deferred income tax assets and an increase of \$18.9 million in long-term income taxes payable. As of the date of adoption, RA's total amount of unrecognized tax benefit was \$23.2 million of which \$7.2 million would affect the effective tax rate, if recognized. We recognize interest accrued and penalties related to unrecognized tax benefits as a component of income tax expense. At the date of adoption, interest accrued and penalties were \$2.2 million. None of the amounts recorded upon adoption of FIN 48 were materially impacted by first quarter 2007 activity.

IRS examinations of Raytheon's consolidated tax returns have been completed for years through 2002 and IRS examinations for tax years 2003 through 2005 began in March 2007. Reports by the IRS Appeals Division ("Appeals") involving various domestic and Foreign Sales Corporation ("FSC") issues for years 1989 through 1997 are awaiting review by the Joint Committee on Taxation. Raytheon has protested to Appeals certain proposed adjustments primarily involving benefits under the FSC and Extraterritorial Income export regimes for years 1998 through 2002. Raytheon's 1984 through 1990 federal research ("R&D") credit refund claim is also under consideration at Appeals. We do not anticipate that the IRS examination or outcome of the FSC and R&D credit appeals process will result in any material adjustments to RA's financial statements.

**Raytheon Aircraft**  
**Notes to Condensed Consolidated Financial Statements**

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**9. Pension & Other Employee Benefits**

RA has several pension and retirement plans covering the majority of its employees, including certain employees in foreign countries (Pension Benefits). In addition to providing Pension Benefits, RA provides certain health care and life insurance benefits to retired employees through other postretirement benefit plans (Other Benefits). Substantially, all of RA's U.S. employees may become eligible for the Other Benefits.

The table below outlines the components of net periodic benefit cost of RA's domestic and foreign Pension Benefits plans.

(In millions)	<b>Three Months Ended</b>	
	<b>March 25, 2007</b>	March 26, 2006
Service cost	<b>\$6.6</b>	\$6.5
Interest cost	<b>13.8</b>	13.1
Expected return on plan assets	<b>(17.1)</b>	(13.7)
Amortization of prior service cost	<b>0.9</b>	1.1
Recognized net actuarial loss	<b>4.2</b>	6.2
<b>Net periodic benefit cost</b>	<b>\$8.4</b>	\$13.2

Net periodic benefit cost includes expense from foreign Pension Benefits plans of \$0.8 million and \$0.7 million for the three months ended March 25, 2007 and March 26, 2006, respectively.

The table below outlines the components of net periodic benefit cost of RA's Other Benefits plan.

(In millions)	<b>Three Months Ended</b>	
	<b>March 25, 2007</b>	March 26, 2006
Service cost	<b>\$0.2</b>	\$0.2
Interest cost	<b>0.2</b>	0.2
Amortization of transition obligation	<b>0.2</b>	0.2
<b>Net periodic benefit cost</b>	<b>\$0.6</b>	\$0.6

Under Statement of Financial Accounting Standards No. 158, Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment to FASB Statement Nos. 87, 88, 106 and 132(R), any previously unrecognized deferred amounts, such as demographic or asset gains or losses and the impact of historical plan changes, are included in accumulated other comprehensive income (loss). These amounts are amortized from accumulated other comprehensive income (loss) to net periodic benefit expense.

RA expects total contributions (required and discretionary) to the Pension Benefits and Other Benefits plans to be approximately \$85.5 million and \$1.0 million, respectively, in 2007. In the three months ended March 25, 2007 and March 26, 2006, Raytheon contributed approximately \$16.2 million and \$11.8 million, respectively, to these plans. Included in the expected funding amounts for 2007 is \$67.2 million funded by Raytheon on March 26, 2007, in accordance with the terms of the purchase agreements.

## Raytheon Aircraft

### Notes to Condensed Consolidated Financial Statements

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#### 10. Commitments and Contingencies

At March 25, 2007 RA had commitments under long-term operating leases requiring approximate annual rentals as follows:

(In millions)	
March 26, 2007 to December 31, 2007	<b>\$6.6</b>
2008	<b>7.0</b>
2009	<b>6.6</b>
2010	<b>4.9</b>
2011	<b>2.6</b>
Thereafter	<b>38.9</b>
Total	<b>\$66.6</b>

Rent expense was \$6.3 million and \$6.4 million for the three months ended March 25, 2007 and March 26, 2006, respectively.

In the normal course of business, RA leases equipment, office buildings, and other facilities under leases that include standard escalation clauses for adjusting rent payments to reflect changes in price indices, as well as renewal options.

RA has committed to construct facilities and purchase equipment under contracts with various third parties. At March 25, 2007, additional payments of \$3.6 million are required under these contracts.

RA has assigned certain leasehold interests to third parties but remain liable to the lessor to the extent the assignee defaults on future lease payments amounting to \$11.7 million at March 25, 2007, extending through 2021.

At March 25, 2007, RA had commitments under an agreement to outsource a significant portion of its information technology function requiring minimum annual payments as follows:

(In millions)	
March 26, 2007 to December 31, 2007	<b>\$12.0</b>
2008	<b>15.7</b>
2009	<b>17.2</b>
2010	<b>4.6</b>
2011	<b>3.4</b>
Thereafter	<b>5.1</b>
Total	<b>\$58.0</b>

In connection with certain aircraft sales, RA has offered trade-in incentives whereby the customer will receive a pre-determined trade-in value if they purchase another aircraft from RA. The difference between the value of these trade-in incentives, the majority of which expire by the end of 2007, and the current estimated fair value of the underlying aircraft was approximately \$1.4 million at March 25, 2007. There is a high degree of uncertainty inherent in determining the likelihood a customer will exercise the incentive.

## Raytheon Aircraft

### Notes to Condensed Consolidated Financial Statements

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RA self-insures for losses and expenses for aircraft product liability up to a maximum of \$10 million per occurrence and \$50 million annually. Insurance is purchased from third parties to cover excess aggregate liability exposure from \$50 million to \$1.25 billion. This coverage also includes the excess of liability over \$10 million per occurrence. The aircraft product liability reserve was \$26.8 million and \$22.3 million at March 25, 2007 and December 31, 2006, respectively.

RA is involved in various stages of investigation and cleanup related to remediation of various environmental sites. RA's estimate of total environmental remediation costs expected to be incurred is \$12.6 million. Discounted at a weighted-average risk-free rate of 6.0%, RA estimates the liability to be \$9.4 million and had this amount accrued in other accrued expenses at March 25, 2007. Due to the complexity of environmental laws and regulations, the varying costs and effectiveness of alternative cleanup methods and technologies, the uncertainty of insurance coverage, and the unresolved extent of RA's responsibility, it is difficult to determine the ultimate outcome of these matters, however, any additional liability is not expected to have a material adverse effect on RA's financial position, results of operations, or liquidity.

RA and Raytheon issue guarantees and have banks and surety companies issue, on their behalf, letters of credit and surety bonds to meet various administrative, bid, performance, warranty, retention and advance payment obligations of RA or its affiliates. Approximately \$14.5 million, \$82.2 million, and \$1.0 million of these guarantees, letters of credit, and surety bonds, for which there were stated values, were outstanding at March 25, 2007, respectively, and \$14.8 million, \$62.4 million, and \$1.2 million were outstanding at December 31, 2006, respectively. These instruments expire on various dates through 2012.

In 2005, RA received an order for 50 Hawker 4000 aircraft and as part of that order RA provided a guaranteed cost of maintenance program for those aircraft. In connection with the order, Raytheon provided the customer an indemnity agreement in support of RA's contractual obligations to both deliver the aircraft and provide the guaranteed cost of maintenance services for ten years after each aircraft is delivered. The indemnity has a stated maximum value of \$125.0 million and is adjusted as aircraft are delivered and the passage of time. Upon completion of the acquisition, this indemnity was terminated upon the mutual consent of the parties involved.

RA is subject to oversight by the FAA. The FAA routinely evaluates aircraft operational and safety requirements and is responsible for certification of new and modified aircraft. Future action by the FAA may adversely affect RA's financial position, results of operations, and liquidity, including recovery of its investment in its newer aircraft.

RA as a defense contractor is subject to many levels of audit and investigation. Agencies that oversee contract performance include: the Defense Contract Audit Agency, the Department of Defense Inspector General, the Government Accountability Office, the Department of Justice, and Congressional Committees. The Department of Justice, from time to time, has convened grand juries to investigate possible irregularities by RA.

In addition, various claims and legal proceedings generally incidental to the normal course of business are pending or threatened against RA. While the ultimate liability or potential range of loss, if any, from these proceedings is presently indeterminable, any additional liability is not expected to have a material adverse effect on RA's financial position, results of operations, or liquidity.

## Raytheon Aircraft

### Notes to Condensed Consolidated Financial Statements

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#### 11. Segment Financial Results

Reportable segments include the following: Business and General Aviation, Trainer Aircraft and Customer Support. Business and General Aviation designs, develops, manufactures, markets, sells and finances commercial and specially modified general aviation aircraft. Trainer Aircraft manufactures and sells military training aircraft to the US and foreign governments. Customer Support provides after-market parts and services support for the in-service aircraft worldwide. Segment net sales include sales to parties affiliated with Raytheon as well as intersegment sales recorded at cost plus a specified fee, which may differ from what the selling entity would be able to obtain on external sales. The Trainer Aircraft segment does not have either related party or intersegment sales.

Segment financial results were as follows:

Net Sales (In millions)	Three Months Ended	
	March 25, 2007	March 26, 2006
Business and General Aviation	\$491.3	\$331.2
Trainer Aircraft	91.2	88.5
Customer Support	135.8	133.5
Eliminations	(50.5)	(48.6)
Total	\$667.8	\$504.6

Sales to affiliated parties for the three months ended March 25, 2007, and March 26, 2006, respectively, were \$17.4 million and \$11.0 million for Business and General Aviation and \$3.1 million and \$13.9 million for Customer Support. Intersegment sales for the three months ended March 25, 2007 and March 26, 2006, respectively, were \$13.5 million and \$13.9 million for Business and General Aviation and \$13.8 million and \$11.7 million for Customer Support.

Operating Income / (Loss) (In millions)	Three Months Ended	
	March 25, 2007	March 26, 2006
Business and General Aviation	\$3.5	\$(7.0)
Trainer Aircraft	12.2	12.3
Customer Support	11.9	3.5
Eliminations	0.8	1.3
Total	\$28.4	\$10.1

#### 12. Recently Issued Accounting Standards

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 establishes a framework for measuring fair value and requires expanded disclosures regarding fair value measurements. This accounting standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. The effect, if any, of adopting SFAS No. 157 on the Business' financial position and results of operations has not yet been determined.

**Raytheon Aircraft**  
**Notes to Condensed Consolidated Financial Statements**

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In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statements No. 115 (SFAS No. 159). SFAS No. 159 permits entities to choose, at specified election dates, to measure eligible items at fair value (the “fair value option”). A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting period. This accounting standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. The effect, if any, of adopting SFAS No. 159 on the Business’ financial position and results of operations has not yet been determined.

## **ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following discussion and analysis of financial condition and results of operations reflects the business of Raytheon Aircraft ("RA"), the predecessor business acquired by Hawker Beechcraft Inc. Unless otherwise indicated, the discussion and analysis does not give effect to the acquisition or include proforma financial adjustments. As discussed in the condensed consolidated financial statements, certain assets and liabilities included in this discussion and analysis were retained by Raytheon Company ("Raytheon") in accordance with the purchase agreement.*

*The following discussion and analysis of RA's financial condition and results of operations should be read in conjunction with and is qualified in its entirety by reference to the condensed consolidated financial statements and accompanying notes included elsewhere in this Form 10-Q. Except for historical information, the discussion in this section includes forward looking statements that involve risks and uncertainties, including but not limited to, those described in the "Risk Factors" section of this Form 10-Q. Future results could differ materially from those discussed below. See discussions under the caption "Cautionary Note Regarding Forward-Looking Statements".*

### **Cautionary Note Regarding Forward-Looking Statements**

Statements that are not reported financial results or other historical information are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. This Form 10-Q includes forward-looking statements including, for example, statements about the terms of the Acquisition (defined below) and the benefits of the Acquisition, our business outlook, the markets in which we operate, including growth of our various markets and our expectations, beliefs, plans, strategies, objectives, prospects, assumptions or future events or performance. These forward-looking statements are not guarantees of future performance. For these statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. These statements are based on management's expectations that involve a number of business risks and uncertainties, any of which could cause actual results to differ materially from those expressed in or implied by the forward-looking statements. In addition to specific factors described in connection with any particular forward-looking statement, factors that could cause actual results to differ materially include, but are not limited to, those discussed under the sections "Risk Factors". All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements set forth or referred to above. We are not obligated to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

### **Presentation of Financial Statements**

On March 26, 2007, subsequent to the closing of RA's fiscal quarter, Hawker Beechcraft Inc. ("HBI") consummated the acquisition (the "Acquisition") of the RA business from Raytheon Company. HBI completed the Acquisition by acquiring all of the outstanding membership interests of Raytheon Aircraft Acquisition Company LLC (which was renamed Hawker Beechcraft Acquisition Company LLC "HBAC") and substantially all of the assets of Raytheon Aircraft Services Limited. Following the Acquisition, HBI contributed the equity interests of the entity purchasing the assets of Raytheon Aircraft Services Limited to HBAC. The business obtained in the Acquisition is essentially the RA business described in Notes 1 and 2 to the condensed consolidated financial statements presented elsewhere in this Form 10-Q. The financial information and other data presented in this Form 10-Q are derived from the combined financial statements of RA. Unless otherwise indicated herein, references to "we", "our", or "us" refer to the RA business essentially acquired.

### **Overview**

RA is a leading designer and manufacturer of business jet, turboprop and piston aircraft. With over 75 years of experience, we believe we are one of the most respected and established manufacturers of general aviation aircraft. Our Hawker and Beechcraft brands have long stood for innovation, performance, quality and value and support the leading market positions of our aircraft.

We have three operating segments—Business and General Aviation, Trainer Aircraft and Customer Support. The Business and General Aviation segment includes all commercial and special mission aircraft sales as well as intercompany sales of aircraft parts to our Customer Support segment. Our Trainer Aircraft segment manufactures our primary military trainer aircraft, the T-6A. In 1995, we were awarded the U.S. Air Force and the U.S. Navy’s Joint Primary Aircraft Training System (“JPATS”) program. Under this contract, we are the sole source provider to the U.S. Air Force and the U.S. Navy of their primary military trainer aircraft. Our Customer Support segment principally provides parts, maintenance and flight support services for our installed fleet. Support is provided to owners of aircraft located around the world by company-owned and company-authorized third-party service centers.

### **Selected Factors Affecting Our Results of Operations**

The general aviation aircraft industry has historically been a cyclical industry that is impacted by many factors including the strength of the U.S. and global economies, corporate profits and geo-political events. In the last few years, the industry has shown consistent growth driven in large part by strong global economic conditions, growth in fractional ownership demand and increasing international acceptance of, and demand for, general aviation aircraft. We believe that changes in deliveries of general aviation aircraft typically lag changes in general economic conditions and corporate profits.

We believe that demand for products and services provided by our Customer Support and Trainer Aircraft segments are less susceptible to changes in economic conditions and provide us with a stable and recurring source of revenues. Our Customer Support business is driven by the size and age of our installed fleet and overall maintenance requirements for our aircraft. Our Trainer Aircraft business is driven largely by government and defense spending and decreases or reprioritization of such spending could affect the performance of this segment.

### **Principal Statement of Operations Items**

***Sales.*** We generate our sales primarily from the sale of aircraft, parts and services to a wide array of customers including corporations, fractional and charter operators, the U.S. and foreign governments and individuals.

***Cost of Sales.*** Our most significant components of cost of sales are purchased components and raw materials, direct labor cost associated with the manufacture of aircraft and parts, and fixed and variable manufacturing overhead expense related to our manufacturing operations.

***Selling, General and Administrative Expenses.*** Selling, general and administrative expenses consist primarily of sales and marketing (including sales commissions, airplane demonstrations and advertising) and corporate expenses (including executive management, treasury, accounting, finance, tax, information technology, human resources, legal, environmental, governance and insurance).

***Research and Development Expenses.*** Expenditures for research and development projects are expensed as incurred. Our research and development expenses consist primarily of labor and associated engineering overhead costs.

***Non-operating Expense, net.*** Non-operating expense, net represents intercompany interest net of external interest income and other income. As a subsidiary of Raytheon, we did not have independent third party borrowings and, as a result, interest expense was not significant. Instead we relied upon Raytheon to finance operations and were allocated an intercompany interest charge.

***Provision for Income Taxes.*** RA’s operating results have historically been included in Raytheon’s consolidated U.S. federal tax return. The provision for income taxes in the financial statements has been determined as if the entities that comprise the business were stand-alone entities and filed separate income tax returns.

## Comparison of the Quarter Ended March 25, 2007 to the Quarter Ended March 26, 2006

### *Consolidated Overview*

**Sales.** Sales were \$667.8 million for the quarter ended March 25, 2007 compared to \$504.6 million for the quarter ended March 26, 2006, an increase of \$163.2 million, or 32.3%. Our sales increased primarily as a result of both higher new and used aircraft deliveries, particularly the Premier and King Air models, and the product mix in our Business and General Aviation segment as detailed below. The Premier deliveries increased during the quarter due to a delay of 14 aircraft deliveries from the fourth quarter of 2006 to 2007. The delay resulted from the timing of approval by the FAA of revisions to the required operating manuals which was received in January 2007.

<b>New Aircraft Delivery Units</b>	<b>First Quarter</b>		<b>Variance</b>
	<b>2006</b>	<b>2007</b>	
<b>Hawker 4000</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Hawker 800XP/850XP</b>	<b>8</b>	<b>10</b>	<b>2</b>
<b>Hawker 400XP</b>	<b>10</b>	<b>7</b>	<b>(3)</b>
<b>Premier</b>	<b>4</b>	<b>15</b>	<b>11</b>
<b>King Airs</b>	<b>22</b>	<b>28</b>	<b>6</b>
<b>Pistons</b>	<b>24</b>	<b>19</b>	<b>(5)</b>
<b>JPATS T-6A</b>	<b>15</b>	<b>9</b>	<b>(6)</b>
<b>Totals</b>	<b>83</b>	<b>88</b>	<b>5</b>

**Cost of Sales.** Cost of sales was \$566.1 million, or 84.8% of sales, for the quarter ended March 25, 2007, compared to \$431.5 million, or 85.5% of sales, for the quarter ended March 26, 2006. The decrease as a percentage of sales was due to a shift in the product mix of aircraft delivered and continued operational efficiencies generated by a higher volume of units produced and on-going efforts to reduce operating costs.

**Selling, General and Administrative.** Selling, general and administrative expenses were \$52.0 million, or 7.8% of sales, for the quarter ended March 25, 2007, compared to \$44.8 million, or 8.9% of sales, for the quarter ended March 26, 2006. This increase in expense resulted primarily from an increase in sales and marketing costs in support of forecast deliveries for the balance of the year and higher headcount in our customer service operations.

**Research and Development Expenses.** Research and development expenses were \$21.3 million, or 3.2% of sales, for the quarter ended March 25, 2007 compared to \$18.2 million, or 3.6% of sales, for the quarter ended March 26, 2006. The increase in expenses reflects the increased certification activity associated with the Hawker 900XP, Hawker 750, King Air 200GT and C90GTi derivative programs.

**Operating Income.** Operating income was \$28.4 million, or 4.3% of sales, for the quarter ended March 25, 2007, compared to \$10.1 million, or 2.0% of sales, for the quarter ended March 26, 2006. The improvement in operating margins reflects increased deliveries and favorable product mix partially offset by higher selling, general and administrative expenses and higher research and development expenses.

**Non-Operating Expense, Net.** Non-operating expense, net was \$14.8 million for the quarter ended March 25, 2007, compared to \$14.9 million for the quarter ended March 26, 2006, a decrease of \$0.1 million. This decrease was primarily as a result of a decrease in intercompany interest allocation offset by lower external interest income and other income.

**Provision for Income Taxes.** The effective rate for the provision for income taxes for the quarter ended March 25, 2007 was 37.5%, compared to 35.4% for the quarter ended March 26, 2006. The increase in the effective tax rate is due to the expiration of certain tax benefits associated with foreign sales.

### Segment Results

The following tables present a comparison of segment sales and operating income for the quarter ended March 25, 2007 to the quarter ended March 26, 2006.

	First Quarter		Change	
	2006	2007		
(In millions)				
<b>Sales by Segment:</b>				
Business and General Aviation .....	\$ 331.2	\$ 491.3	\$ 160.1	48.4%
Trainer Aircraft .....	88.5	91.2	2.7	3.1%
Customer Support .....	133.5	135.8	2.3	1.7%
Eliminations.....	(48.6)	(50.5)	(1.9)	(3.9%)
Total.....	\$ 504.6	\$ 667.8	\$ 163.2	32.4%

	First Quarter		Change	
	2006	2007		
(In millions)				
<b>Operating Income (Loss) by Segment:</b>				
Business and General Aviation .....	\$ (7.0)	\$ 3.5	\$ 10.5	N/A
Trainer Aircraft .....	12.3	12.2	(0.1)	(0.1%)
Customer Support .....	3.5	11.9	8.4	240.0%
Eliminations.....	1.3	0.8	(0.5)	(38.5%)
Total.....	\$ 10.1	\$ 28.4	\$ 18.3	181.2%

**Business and General Aviation.** Business and General Aviation sales for the quarter ended March 25, 2007 increased \$160.1 million, or 48.4%, over the quarter ended March 26, 2006 due primarily to continued strength in the general aviation market, recent derivative launches and growth in international sales.

Operating income (loss) was \$3.5 million, or 0.7% of sales, for the quarter ended March 25, 2007, compared to \$(7.0) million, or (2.1%) of sales, for the quarter ended March 26, 2006. The increase in operating margins was principally driven by higher unit deliveries, favorable product mix and operational efficiencies generated by a higher volume of units produced and on-going efforts to reduce operating costs.

**Trainer Aircraft.** Trainer Aircraft sales for the quarter ended March 25, 2007 increased by \$2.7 million, or 3.1%, as compared to the quarter ended March 26, 2006.

Operating income was \$12.2 million, or 13.4% of sales, for the quarter ended March 25, 2007, compared to \$12.3 million, or 13.9% of sales, for the quarter ended March 26, 2006. First quarter 2006 operating income included a \$3.4 million favorable adjustment to our contract estimates for our JPATS program while first quarter 2007 only included \$2.3 million of comparable adjustments.

**Customer Support.** Customer Support sales for the quarter ended March 25, 2007 increased by \$2.3 million, or 1.7%, from the quarter ended March 26, 2006.

Operating income was \$11.9 million, or 8.8% of sales, for the quarter ended March 25, 2007, compared to \$3.5 million, or 2.6% of sales, for the quarter ended March 26, 2006. The increase in operating margins was principally due to the termination of the unprofitable, related party Flight Options contract in early 2006 and improved operational performance at our service center and parts businesses.

## **Liquidity and Capital Resources**

### **Historical**

We have historically satisfied our liquidity requirements through a combination of cash generated from operating activities as well as from borrowings from Raytheon. All of our excess cash was remitted to Raytheon. Our future short-term liquidity needs include amounts required for debt service and day-to-day operating expenses such as working capital requirements and the funding of capital expenditures. Our future long-term liquidity requirements include working capital, capital expenditures and debt service.

Cash provided by operating, investing and financing activities for the quarters ended March 25, 2007 and March 26, 2006 are summarized below.

***Quarter Ended March 25, 2007.*** Cash used by operating activities was \$102.1 million. The net cash used was primarily due to the more linear build of commercial aircraft compared to aircraft sales which are more heavily weighted to occur during the second half of the year as well as the on-going liquidation of the T6-A advance payments due to the changed payment terms associated with the program going forward. Partially offsetting these impacts was early pay-off on General Aviation financing receivables.

Cash used in investing activities of \$27.3 million included capital expenditures of \$26.2 million primarily related to company-manufactured tooling and modernizing equipment used in the manufacturing process and \$1.1 million of additions to intangible assets primarily related to investment in software.

Cash provided by financing activities of \$118.6 million represents net transfers from Raytheon.

***Quarter Ended March 26, 2006.*** Cash provided by operating activities was \$22.6 million. The net cash provided by operating activities was primarily due the T6-A Lot 13 contract collection received from our U.S. Government customer and increased collections on notes offset by the more linear build of commercial aircraft compared to aircraft sales which are more heavily weighted to occur during the second half of the year.

Cash used in investing activities of \$8.7 million included capital expenditures of \$8.1 million primarily related to company-manufactured tooling and \$0.6 million of additions to intangible assets primarily related to investment in software.

Cash used by financing activities of \$16.7 million represents net transfers to Raytheon.

### **Prospective**

Following the Acquisition, our principal sources of liquidity consist of cash generated by operations and borrowings under our new revolving credit facility.

In connection with the Acquisition, HBAC issued \$1,100.0 million of notes, including \$400.0 million of 8.5% Senior Fixed Rate Notes due 2015, \$400.0 million 8.875%/9.625% Senior PIK-Election Notes due April 1, 2015 and \$300.0 million of 9.75% Senior Subordinated Notes due April 1, 2017, and entered into senior secured credit facilities totaling \$1,810.0 million, consisting of a \$1,300.0 million term loan drawn at the close of the Acquisition, an undrawn \$400.0 million revolving credit facility and a \$110.0 million synthetic letter of credit facility.

The indentures governing the notes and the credit agreement governing our new senior secured credit facilities contain a number of covenants imposing significant restrictions on our business. These restrictions may affect our ability to operate our business and may limit our ability to take advantage of potential business opportunities as they arise. The restrictions these covenants place on us include limitations on our ability to:

- incur indebtedness or issue disqualified stock or preferred stock;
- pay dividends on, redeem or repurchase our capital stock;
- make investment or acquisitions;
- create liens;
- sell assets;
- engage in sale and leaseback transactions;
- restrict dividends or other payments to us;
- guarantee indebtedness;
- engage in transactions with affiliates; and
- consolidate, merge or transfer all or substantially all of our assets.

Our ability to make payments on and to refinance our indebtedness, including the notes, and to fund planned capital expenditures will depend on our ability to generate cash in the future. This is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control. Our management believes that our cash on hand, together with cash from operations and, if required, borrowings under the multi-currency revolving credit facility of our new senior secured credit facilities, will be sufficient for our cash requirements through at least the remainder of 2007.

### **Commitments and Contingencies**

In connection with certain aircraft sales, RA has offered trade-in incentives whereby the customer will receive a pre-determined trade-in value if they purchase another aircraft from RA. The difference between the value of these trade-in incentives, the majority of which expire by the end of 2007, and the current estimated fair value of the underlying aircraft was approximately \$1.4 million at March 25, 2007. There is a high degree of uncertainty inherent in determining the likelihood a customer will exercise the incentive.

RA self-insures for losses and expenses for aircraft product liability up to a maximum of \$10 million per occurrence and \$50 million annually. Insurance is purchased from third parties to cover excess aggregate liability exposure from \$50 million to \$1.25 billion. This coverage also includes the excess of liability over \$10 million per occurrence. The aircraft product liability reserve was \$26.8 million and \$22.3 million at March 25, 2007 and December 31, 2006, respectively.

RA is involved in various stages of investigation and cleanup related to remediation of various environmental sites. RA's estimate of total environmental remediation costs expected to be incurred is \$12.6 million. Discounted at a

weighted-average risk-free rate of 6.0%, RA estimates the liability to be \$9.4 million and had this amount accrued in other accrued expenses at March 25, 2007. Due to the complexity of environmental laws and regulations, the varying costs and effectiveness of alternative cleanup methods and technologies, the uncertainty of insurance coverage, and the unresolved extent of RA's responsibility, it is difficult to determine the ultimate outcome of these matters, however, any additional liability is not expected to have a material adverse effect on RA's financial position, results of operations, or liquidity. Raytheon retained a significant portion of the liability associated with environmental remediation in accordance with the purchase agreement related to the Acquisition.

RA and Raytheon issue guarantees and have banks and surety companies issue, on their behalf, letters of credit and surety bonds to meet various administrative, bid, performance, warranty, retention and advance payment obligations of RA or its affiliates. Approximately \$14.5 million, \$82.2 million, and \$1.0 million of these guarantees, letters of credit, and surety bonds, for which there were stated values, were outstanding at March 25, 2007, respectively, and \$14.8 million, \$62.4 million, and \$1.2 million were outstanding at December 31, 2006, respectively. These instruments expire on various dates through 2012.

In 2005, RA received an order for 50 Hawker 4000 aircraft and as part of that order RA provided a guaranteed cost of maintenance program for those aircraft. In connection with the order, Raytheon provided the customer an indemnity agreement in support of RA's contractual obligations to both deliver the aircraft and provide the guaranteed cost of maintenance services for ten years after each aircraft is delivered. The indemnity has a stated maximum value of \$125.0 million and is adjusted as aircraft are delivered and the passage of time. Upon completion of the acquisition, this indemnity was terminated upon the mutual consent of the parties involved.

#### **Recently Issued Accounting Standards**

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 establishes a framework for measuring fair value and requires expanded disclosures regarding fair value measurements. This accounting standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. The effect, if any, of adopting SFAS No. 157 on the Business' financial position and results of operations has not yet been determined.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statements No. 115 (SFAS No. 159). SFAS No. 159 permits entities to choose, at specified election dates, to measure eligible items at fair value (the "fair value option"). A business entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting period. This accounting standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. The effect, if any, of adopting SFAS No. 159 on the Business' financial position and results of operations has not yet been determined.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

#### **Historical**

Under our historical capital structure, our primary market exposure was to foreign exchange rates. Our sales are denominated primarily in U.S. dollars. As a result of contracts with certain suppliers, we have expenses that are denominated in British pounds sterling. As a result, movements in exchange rates could cause our expenses to fluctuate, impacting our profitability and cash flows. We use foreign currency forward contracts to reduce our exposure to currency exchange rate fluctuations. The objective of these contracts is to minimize the impact of currency exchange rate movements on our operating results. We do not use these contracts for speculative or trading purposes. We believe our exposure due to changes in foreign currency exchange rates is not material due to our hedging policy and the fact that we do not enter into speculative hedges.

#### **Prospective**

Following the Acquisition, we are subject to interest rate market risk in connection with our long-term debt. Our principal interest rate exposure relates to outstanding amounts under our new senior secured credit facilities. Our new senior secured credit facilities provide for variable rate borrowings of up to \$1,700.0 million including availability of \$400.0 million under our revolving credit facility. Assuming the senior secured credit facilities are fully drawn, each one-eighth percentage point increase or decrease in the applicable interest rates would correspondingly change our interest expense on the senior secured credit facilities by approximately \$2.1 million per year. In the future, we may enter into interest rate swaps to reduce interest rate volatility.

### **ITEM 4. CONTROLS AND PROCEDURES**

This section is not currently applicable to our business.

## **PART II. OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

RA is involved in various stages of investigation and cleanup relative to remediation of various environmental sites. All appropriate costs expected to be incurred in connection therewith have been accrued. Due to the complexity of environmental laws and regulations, the varying costs and effectiveness of alternative cleanup methods and technologies, the uncertainty of insurance coverage and the unresolved extent of our responsibility, it is difficult to determine the ultimate outcome of these matters. However, in the opinion of management, any liability is not expected to have a material effect on our financial position, liquidity or results of operations. Raytheon retained a significant portion of the liability associated with environmental remediation in accordance with the purchase agreement related to the Acquisition.

Various other claims and legal proceedings generally incidental to the normal course of business are pending or threatened on behalf of or against us. While we cannot predict the outcome of these matters, in the opinion of management, any liability arising from them is not expected to have a material effect on our financial position, liquidity or results of operations after giving effect to provisions already recorded.

### **ITEM 1A. RISK FACTORS**

*The risks described below are not the only risks we face. Additional risks not presently known to us or which we currently consider immaterial also may adversely affect us. In any of these risks or uncertainties actually occurs, our business, financial condition and operating results could be materially adversely affected.*

***Our results of operations and financial condition could be adversely affected by a downturn in the general aviation and other aircraft markets or the general economic environment.***

Our results of operations and financial condition depend on a number of factors, including general economic conditions, such as the availability and cost of fuel, and demand for new and used business jets, spare parts and maintenance. If there is a downturn in the general aviation and other aircraft markets due to such conditions, our results of operations and financial condition could be negatively impacted.

Aircraft customers, including sellers of fractional share interests, may respond to weak economic conditions by delaying delivery of orders or canceling orders. We could subsequently experience declining sales of aircraft and increases in aircraft inventories and costs. Weakness in the economy may also result in fewer hours being flown on existing aircraft and, consequently, lower demand for spare parts and maintenance services. Weak economic conditions may also cause reduced demand for used business jets. We may accept used aircraft on trade-in that would be subject to reductions in the fair market value of the aircraft while in inventory.

Further, the products we sell are considered discretionary purchases and our levels of sales have historically been tied to corporate and consumer spending levels, which are typically cyclical in nature. Our sales are significantly impacted by the level of corporate spending primarily in North America which, in turn, is a function of the general economic environment. In a recessionary economy, corporate cash flows decrease which typically leads to a decrease in demand for our products or postponement of planned purchases. The purchase of our products by consumers is discretionary, and therefore highly dependent upon the level of consumer spending. Accordingly, sales of our products may be adversely affected by an economic downturn, increases in consumer debt levels, uncertainties regarding future economic prospects or a decline in consumer confidence.

***Our business has historically been seasonal.***

Historically, our peak deliveries have occurred during the last quarter of the calendar year. For example, inclement weather conditions during that time of year may impair our ability to conduct necessary pre-delivery flight tests and/or deliver aircraft, and may adversely affect our financial results.

***A significant decline in business with NetJets could adversely affect our business and financial results.***

Currently, NetJets is the largest customer in our Business and General Aviation segment, accounting for a significant percentage of our backlog and commercial aircraft sales. Our contracts with NetJets permit it to terminate the contracts or cancel any or all aircraft orders at any time, subject to payment of liquidated damages under certain circumstances. A significant reduction in purchases by NetJets could have a material adverse effect on our financial condition, results of operations and cash flows. If NetJets: (1) experiences a decrease in requirements for the products which we supply to it; (2) experiences a major disruption in its business or a decrease in orders from its customers; (3) suffers operational or financial difficulties; or (4) becomes dissatisfied with the level and/or quality of service we provide, we believe that our business, financial condition and results of operations could be materially adversely affected.

***Our JPATS contracts expose us to the inherent risks of fixed price contracting and future contracts under the JPATS program are not guaranteed.***

We manufacture aircraft for the U.S. Air Force, the U.S. Navy and international governments. We provide some of our products and services through long-term contracts in which the pricing terms are fixed based on certain production volumes. For instance, in 2007, HawkerBeechcraft anticipates being awarded the JPATS lots 14-16 contract which will require delivery of 195 aircraft through 2012. In addition, we expect lots 17-20 for 153 aircraft deliveries to be awarded in 2010 with deliveries through 2015. Since these contracts are fixed price contracts, we bear the risk that increased or unexpected costs may reduce our profit margins or cause us to sustain losses on these contracts. We must fully absorb cost overruns, notwithstanding the difficulty of estimating all of the costs we will incur in performing these contracts and in projecting the ultimate level of sales that we may achieve. Our failure to anticipate technical problems, estimate delivery reductions, estimate costs accurately or control costs during performance of a fixed price contract may reduce the profitability of a contract or cause a loss.

Government programs such as the JPATS program are generally implemented by the award of multi-year contracts in which the pricing for future years' procurements by the government is negotiated under fixed price contracts and segregated into individual lots to be exercised on an annual basis. The award of these future lots is subject to future Congressional appropriations. Congress generally appropriates funds on a fiscal year basis even though a program extends for more than one year. Consequently, programs are often only partially funded at any one time, and additional funds are committed only as Congress makes further appropriations. U.S. government contracts under such a program are subject to termination or adjustment if appropriations for such program are not available or change. In addition, U.S. government contracts, including the JPATS contract, generally contain provisions permitting termination, in whole or in part, without prior notice at the U.S. government's convenience as well as termination for default based on performance. Upon termination for convenience, we are generally entitled to compensation only for work done and commitments made at the time of termination. A termination arising out of our default could expose us to liability and have a negative impact on our ability to obtain future contracts and orders. Furthermore, on contracts for which we are a subcontractor and not the prime contractor, the U.S. government could terminate the prime contract for convenience or otherwise, irrespective of our performance as a subcontractor.

The termination of one or more large contracts, whether due to lack of funding, for convenience, or otherwise, or the occurrence of delays, cost overruns and product failures in connection with one or more government contracts, could negatively impact our results of operations and financial condition. Furthermore, we can give no assurance that we would be able to procure new U.S. government contracts to offset the revenues lost as a result of any termination of our current U.S. government contracts. Substantially all of our Trainer Aircraft segment sales are from our JPATS contract. A termination of the JPATS contract would substantially reduce future sales in this segment.

We were originally awarded the JPATS contract under the Federal Acquisition Regulation ("FAR"), Part 12, which provided for significant advance payments. Our new contract covering lots 14-16 will be awarded under FAR, Part 15, which provides for payments based on expenditures. The completion of lot 13 and transition to lot 14 will have a temporary adverse effect on our cash flow due to the reduction of the cash advance payment balance as lot 13 is completed and changes in the timing and receipt of customer payments as compared to previous contracts awarded under the JPATS program.

***We operate in a very competitive business environment.***

The general aviation industry is highly competitive and we encounter competition in both domestic and foreign markets. The highly competitive nature of our industry means we are continually subject to the risk of loss of our market share, loss of significant customers, reduction in margins, the inability for us to gain market share or acquire new customers, and difficulty in raising our prices.

***We are at risk of losses and adverse publicity stemming from any accident involving aircraft for which we hold design authority.***

If an RA product were to crash or be involved in an accident, we could be exposed to significant tort liability. We are currently involved in various litigation matters stemming from such incidents. Above our self insured amounts, our insurance may be inadequate to cover damages arising from any future accidents. In the event that our insurance is not adequate, we may be forced to bear substantial losses from an accident. In addition, any accident involving RA could create a public perception that our aircraft are not safe or reliable, which could harm our reputation and negatively impact our financial results.

The General Aviation Revitalization Act of 1994 (“GARA”) provides certain limitations on liability for manufacturers of aircraft and components that have been in service for 18 years; however, such limitations on liability are dependant upon the facts and circumstances surrounding the incident giving rise to liability. Furthermore, RA has manufactured certain aircraft that remain in operation, including the King Air 1900, that may not be covered by GARA at all. As a result, if any of these aircraft were to crash or be involved in an accident, we could be exposed to tort liability and may not have a defense under GARA.

Furthermore, accidents and incidents involving RA aircraft may prompt the FAA to issue airworthiness directives or other notices regarding the aircraft, and we have received such airworthiness directives regarding RA aircraft previously. Publication of an FAA airworthiness directive or notice could create a public perception that a particular RA aircraft is not safe, reliable, or suitable for an operator’s needs. This perception could result in a claim being filed against us or lost future sales, or both. In addition, the FAA could require design modifications causing us to incur significant expenditures altering an aircraft design, altering aircraft in production and altering fielded aircraft under warranty. FAA airworthiness directives are typically followed by similar regulatory requirements in other countries where affected aircraft are certified. The publication of any of the foregoing by the FAA could lead to a decline in revenues and have a negative impact on our business, financial condition and results of operations.

***The outcome of litigation in which we have been named as a defendant is unpredictable and an adverse decision in any such matter could have a material adverse effect on our financial position, results of operations and liquidity.***

We are defendants in a number of litigation matters and are subject to various other claims, demands and investigations. These matters may divert financial and management resources that would otherwise be used to benefit our operations. No assurances can be given that the results of these matters will be favorable to us. An adverse resolution or outcome of any of these lawsuits, claims, demands or investigations could have a negative impact on our business, financial condition, results of operations and liquidity.

***We incur risks associated with our new programs.***

The principal markets in which our businesses operate experience changes due to the introduction of new technologies. To meet our customers’ needs in these businesses, we must continuously design new products, update existing products and services, and invest in and develop new technologies. New programs with new technologies typically carry risks associated with design responsibility, FAA mandated certification requirements, development of new production tools, hiring and training of qualified personnel, increased capital and funding commitments, delivery schedules and unique contractual requirements, supplier performance, and our ability to accurately estimate costs associated with such programs. Our competitors may also develop products that are superior to our products or may adapt more quickly than us to new technologies or evolving customer requirements. Technological advances by our competitors may lead to new manufacturing techniques to make their products and make it more difficult for us to compete. In addition, any new aircraft program may not generate sufficient demand or may experience technological problems or significant delays in the regulatory certification or manufacturing and delivery schedule and the costs of these new aircraft programs may exceed our expectations. If we were unable to manufacture products at our estimated costs or if a new program in which we had made a significant investment experienced

weak demand, delays or technological problems, our business, financial condition and results of operations could be materially adversely affected.

There are a number of risks inherent in our new platform and derivatives introductions which could negatively impact our sales. Also, introduction costs and manufacturing inefficiencies may be greater than anticipated, which could impact our profitability. For example, we plan to begin deliveries of our new Hawker 4000 during the second half of 2007. As this aircraft has no sales history, its reliability, dependability and operations remain unknown. We have also entered into fixed price maintenance and dispatch reliability contracts for this aircraft and, because it has no operating history, we may underestimate the actual costs of maintenance. In addition, the commercial delivery schedule remains subject to change and is dependent upon receipt of a production certificate from the FAA. While we cannot predict the outcome of decisions by the FAA, we currently expect to receive final approval to allow us to commence commercial deliveries of the Hawker 4000 during the second half of 2007. There is a risk that a delay in production or delivery may cause customers to cancel their orders for the Hawker 4000.

***Our operations depend on our ability to maintain continuous, uninterrupted production at our manufacturing facilities. Our production facilities are subject to physical and other risks that could disrupt production.***

Our manufacturing facilities could be damaged or disrupted by a natural disaster, war, terrorist activity or sustained mechanical failure. Although we have obtained property damage and business interruption insurance in amounts determined sufficient by management, a major catastrophe, such as a fire, flood, tornado or other natural disaster at any of our sites, war or terrorist activities in any of the areas where we conduct operations or the sustained mechanical failure of a key piece of equipment could result in a prolonged interruption of all or a substantial portion of our business. Any disruption resulting from these events could cause significant delays in shipments of products and the loss of sales and customers; we may not have insurance to adequately compensate us for any of these events. A large portion of our operations takes place at facilities in Wichita and Salina, Kansas and in Little Rock, Arkansas and any significant damage or disruption to these facilities in particular would materially adversely affect our ability to manufacture and deliver aircraft and parts to our customers.

***Any significant disruption in our supply from key vendors could delay production and adversely affect our sales.***

We are highly dependent on the availability of essential materials and purchased components from our suppliers, some of which are available only from a sole source or limited sources. Moreover, we are dependent upon the ability of our suppliers to provide material and components that meet specifications, quality standards and delivery schedules. Our suppliers' failure to provide expected raw materials or component parts could adversely affect production schedules and contract profitability.

We have from time to time experienced limited interruptions of supply but we may experience a serious interruption in the future. Our continued supply of materials is subject to a number of risks including:

- the destruction of our suppliers' facilities or their distribution infrastructure;
- a work stoppage or strike by our suppliers' employees;
- the failure of our suppliers to provide materials of the requisite quality;
- the failure of essential equipment at our suppliers' plants;
- the failure of our foreign suppliers to satisfy U.S. import or export control laws for goods that we purchase from such suppliers;
- the failure of suppliers to meet regulatory standards;
- the failure, shortage or delays in the delivery of supply of raw materials to our suppliers; and
- contractual amendments and disputes with our suppliers.

In addition, contracts with certain of our suppliers for raw materials and other goods are short-term contracts. We cannot assure you that these suppliers will continue to provide products to us at attractive prices or at all, or that we will be able to obtain such products in the future from these or other providers on the scale and within the time periods we require. Our foreign suppliers must also comply with U.S. import/export control laws. Any failure to comply with such laws may delay or halt production. For example, recently the supplier of one of the major components of our T-6A Trainer suspended shipments pending resolution of an import/export law compliance

matter. If we are not able to obtain key products on a timely basis and at affordable costs, or we experience significant delays or interruptions of their supply, it could have a material adverse effect on our business, financial condition and results of operations.

Further, the FAA prescribes standards and qualification requirements for aerostructures, including virtually all general aviation products, with which our suppliers must comply. We cannot assure you that our suppliers will be able to comply and failure to do so may cause shortages or delays. We cannot assure you that substitute raw materials or component parts will be available to us or will meet the strict specifications and quality standards we, our customers and the U.S. government impose. Often, our certification from the FAA relates to a specific part from a specific supplier. If we were forced to certify replacement parts from a new vendor, the certification process could materially delay production and adversely affect our business, financial condition and results of operations.

***Increases in labor costs, potential labor disputes and work stoppages at our facilities could materially adversely affect our financial performance.***

Our financial performance is affected by the availability of qualified personnel and the cost of labor. Approximately half of our hourly workforce are represented by unions. If our workers were to engage in a strike, work stoppage or other slowdown, we could experience a significant disruption of our operations that could cause us to be unable to deliver products to our customers on a timely basis and could result in a breach of our supply agreements. This could result in a loss of business and an increase in our operating expenses, which could have a material adverse effect on our business, financial condition and results of operations. In addition, our non-unionized labor force may become subject to labor union organizing efforts, which could cause us to incur additional labor costs and increase the related risks that we now face.

***Our business will suffer if we are unable to recruit and retain highly skilled staff.***

The success of our business is highly dependent upon our ability to continue to recruit, train and retain skilled employees, particularly skilled engineers. The market for these resources is highly competitive. We may be unsuccessful in attracting and retaining the engineers we need at economically competitive prices or at all, and, in such event, our business could be materially adversely affected. Our inability to hire new personnel with the requisite skills could impair our ability to provide products to our customers or to manage our business effectively.

***We are subject to government regulation and our business may be materially adversely affected if we lose our government, regulatory or industry approvals, if more stringent government regulations are enacted or if industry oversight is increased.***

The FAA prescribes standards and qualification requirements for aerostructures, including virtually all general aviation products. Comparable agencies, including but not limited to the European Aviation Safety Agency (the "EASA"), in Europe, regulate these matters in other countries. If we fail to qualify for or obtain a required license for one of our products or services or lose a qualification or license previously granted, the sale of the subject product or service would be prohibited by law until such license is obtained or renewed and our business, financial condition and results of operations could be materially adversely affected. In addition, designing new products to meet existing regulatory requirements and retrofitting installed products to comply with new regulatory requirements can be expensive and time consuming.

From time to time, the FAA, the EASA or comparable agencies propose new regulations or changes to existing regulations. These changes or new regulations generally increase the costs of compliance. To the extent the FAA, the EASA or comparable agencies implement regulatory changes, we may incur significant additional costs to achieve compliance.

Further, our business could be materially adversely affected if the U.S. government enacts new regulation in the form of "user fees" or other tax regulation on our products or their use. Our products are generally considered discretionary goods and are not currently subject to "user fees" or other excess taxation. If the U.S. government were to institute new taxes on the operation or use of our products, the attractiveness of general aviation as an alternative to commercial airfare could be affected and demand for our products may decrease. Any one or more of such U.S. government regulation or taxation programs could have a material adverse effect on our business, financial condition and results of operations.

***We are subject to regulation of our technical data and goods under U.S. export control laws.***

The FAA prescribes standards and qualification requirements for aerostructures and the production thereof, including virtually all general aviation products. The FAA further regulates virtually all aviation services, such as maintenance, training, the operation of aircraft, and the provision of charter services. Comparable agencies include, but are not limited to, the International Traffic in Arms Regulations administered by the U.S. Department of State, and the Export Administration Regulations administered by the U.S. Department of Commerce. Collaborative agreements that we may have with foreign persons, including manufacturers and suppliers, are also subject to U.S. export control laws. In addition, we are subject to trade sanctions against embargoed countries, administered by the Office of Foreign Assets Control within the U.S. Department of the Treasury.

A determination that we have failed to comply with one or more of these export controls or trade sanctions could result in civil or criminal penalties, including the imposition of fines upon us as well as the denial of export privileges and debarment from participation in U.S. government contracts. Delays or disapproval of export or import licenses or agreements could delay production and adversely affect our financial condition. Additionally, restrictions may be placed on the export of technical data and goods in the future as a result of changing geo-political conditions. Any one or more of such sanctions could have a material adverse effect on our business, financial condition and results of operations.

***We are subject to strict environmental laws and regulations that may lead to significant, unforeseen expenses.***

Our operations are subject to the requirements of federal, state, local, European and other foreign environmental and occupational health and safety laws and regulations, the violation of which can result in substantial costs and liabilities, including material civil and criminal fines and penalties. Such requirements include those pertaining to pollution; the protection of human health and the environment; air emissions; wastewater discharges; occupational safety and health; and the generation, handling, treatment, remediation, use, storage, transport, release of and exposure to, hazardous substances and wastes. We have incurred and will continue to incur costs and capital expenditures to comply with these environmental requirements and to obtain and maintain all necessary permits. Any failure by us to comply with such laws and regulations could subject us to significant civil or criminal fines and penalties and other liabilities. In addition, if we were convicted of a violation of certain of these laws or regulations (including the Clean Air Act and the Clean Water Act), we, or one of our subsidiaries, could be placed by the United States Environmental Protection Agency (the "EPA") under 40 CFR Part 32 on the "Excluded Parties List" maintained by the Government Services Administration. The listing would continue until the EPA concluded that the cause of the violation had been cured. Facilities at which the violation occurred cannot be used in performing any U.S. government contract awarded during any period of listing by the EPA, and pre-existing contracts may be terminated by the government once a facility is listed. In addition, this prohibition can also extend to other facilities that are owned or operated by the convicted person.

Under certain of these laws and regulations, such as the federal Superfund statute, the obligation to investigate and remediate contamination at a facility may be imposed on current and former owners or operators or on persons who may have sent waste to that facility for disposal. Liability under these laws and regulations may be without regard to fault or to the legality of the activities giving rise to the contamination. Contamination has been identified at some of our facilities, and we have incurred, and will continue to incur, costs to investigate and remediate these conditions. In connection with such contamination, we may also be liable for natural resource damages, government penalties and claims by third parties for personal injury and property damage. In addition, we may incur liabilities in connection with any future environmental contamination or any previously unknown but currently existing environmental conditions at our facilities. The costs of investigation, remediation and other costs with respect to identified environmental conditions, including conditions at offsite disposal locations with respect to which we have been notified of potential liability, could be significant.

In addition, environmental laws and regulations, and the interpretation or enforcement thereof, are constantly evolving and it is impossible to predict accurately the effect that changes in these laws and regulations, or their interpretation or enforcement, may have upon our business, financial condition or results of operations. Should environmental laws and regulations, or their interpretation or enforcement thereof become more stringent, the costs of compliance could increase. If we cannot pass along future cost increases to our customers, any such increases may have an adverse effect on our business, financial condition or results of operations.

***We derive a significant portion of our revenues from direct and indirect sales outside the United States and are subject to the risks of doing business in foreign countries.***

We derive a significant portion of our revenues from sales to customers outside the United States. We expect that our international sales will continue to account for a significant portion of our revenues for the foreseeable future and will increase over time. As a result, we are subject to risks of doing business internationally, including:

- changes in regulatory requirements;
- domestic and foreign government policies, including requirements to expend a portion of program funds locally and governmental industrial cooperation requirements;
- the complexity and necessity of using foreign representatives and consultants;
- fluctuations in foreign currency exchange rates;
  
- lack of intellectual property protection in foreign jurisdictions;
- imposition of tariffs or embargoes, export controls and other trade restrictions;
- the difficulty of management and operation of an enterprise spread over various countries;
- compliance with a variety of foreign laws, as well as U.S. laws affecting the activities of U.S. companies abroad; and
- economic and geopolitical developments and conditions, including international hostilities, political instability, acts of terrorism and governmental reactions, inflation, trade relationships and military and political alliances.

While these factors or the impact of these factors are difficult to predict, adverse developments of any one or more of these factors could materially adversely affect our business, financial condition and results of operations in the future.

In order to sell many of our products outside of the United States, we must first obtain licenses and authorizations from various government agencies. For certain sales of defense equipment and services to foreign governments, the U.S. Department of State must notify Congress at least 15 to 30 days, depending on the size and location of the sale, prior to authorizing these sales. During that time, Congress may take action to block the proposed sale. We can give no assurance that we will continue to be successful in obtaining the necessary licenses or authorizations or that Congress will not prevent certain sales. Our inability to sell products outside of the United States could negatively impact our results of operations and financial condition.

***We must assess the value of used aircraft and aircraft materials and parts, which requires significant judgment, and changes in the value of such items could adversely affect our future financial results.***

The valuation of used aircraft in inventory, which are stated at cost, but not in excess of realizable value, requires significant judgment. As part of our assessment of realizable value, we evaluate many factors, including current and future market conditions, the age and condition of the aircraft and availability levels of the aircraft in the market. In addition, the valuation of aircraft materials and parts that support our worldwide fleet of aircraft, which are stated at cost, but not in excess of realizable value, also requires significant judgment. As part of our assessment of realizable value, we evaluate many factors, including the expected useful life of the aircraft, some of which have remained in service for up to 75 years. Furthermore, we assume an orderly disposition of both used aircraft and aircraft materials and parts in connection with our assessments of realizable value. Changes in market or economic conditions and changes in products or competitive products may adversely impact the future valuation of used aircraft and aircraft materials and parts and such changes in valuation could negatively impact our future financial condition and results of operations.

***We accept used aircraft as trade-ins from our customers and may be required to accept trade-ins at a financial loss.***

In connection with the signing of a purchase contract for new aircraft, we may agree to accept a trade-in aircraft from our customer as partial consideration of the purchase price. We attempt to value trade-ins at levels that will allow us to dispose of the used aircraft in 60 to 90 days. For certain aircraft with long delays between signing of a purchase contract and actual delivery of the aircraft, we may be required to accept trade-ins at prices that are above

the then market price of the aircraft, which would result in lower operating margins at the time of the new aircraft sale.

Any future decrease in the market value of the aircraft we accept on trade-in could cause us to incur charges to income. We cannot assure you that then-prevailing market conditions would allow us to resell or lease the underlying used aircraft at its anticipated fair value or in a timely manner. Consequently, our practice of accepting trade-ins of aircraft from our customers could reduce our cash flow in a particular year.

Trade-in activity varies significantly by aircraft model. Depending on the model of new aircraft sold, approximately 29 percent to 55 percent of new units sold over the past five years involved a trade-in of a used aircraft.

***Our business could be adversely affected by a negative audit by the U.S. government.***

As a government contractor we are subject to routine audits and investigations by U.S. government agencies such as the Defense Contract Audit Agency (the “DCAA”). These agencies review a contractor’s performance under its contracts, cost structure and compliance with applicable laws, regulations and standards. The DCAA also reviews the adequacy of, and a contractor’s compliance with, its internal control systems and policies, including the contractor’s purchasing, property, estimating, compensation and management information systems. Any costs found to be improperly allocated to a specific contract will not be reimbursed or must be refunded if already reimbursed. Moreover, private individuals may bring qui tam, or “whistle blower” suits, under the False Claims Act, which permits a private individual to bring a claim on behalf of the U.S. government to recover payments made as a result of a false claim. Such individuals may receive a portion of amounts recovered on behalf of the U.S. government. If an audit uncovers improper or illegal activities, we may be subject to civil and criminal penalties and administrative sanctions, which may include: termination of contracts; forfeiture of profits; suspension of payments; fines; and suspension or prohibition from doing business with the U.S. government. In addition, we could suffer serious reputational harm if allegations of impropriety were made against us.

***Our business operations could be negatively impacted if we fail to adequately protect our intellectual property rights or if third parties claim that we are in violation of their intellectual property rights.***

We rely on a combination of trademarks, copyrights, patents, non-patented, proprietary know-how, trade secrets and other proprietary information. We employ various methods to protect our proprietary information, including confidentiality agreements, invention assignment agreements and proprietary information agreements with vendors, employees, contractors, distributors, consultants and others. However, these agreements may be breached. In addition, we hold U.S. and foreign trademarks and patents relating to a number of our products and have additional trademark and patent applications pending. We also apply for patents in the ordinary course of our business, as we deem appropriate. However, these precautions offer only limited protection, and our proprietary information may become known to, or be independently developed by, competitors, patent or trademark applications might not be issued, or our proprietary rights in intellectual property may be challenged, any of which could have a material adverse effect on our business, financial condition and results of operations. Additionally, our existing or future patents, if any, may not afford us significant competitive advantage, and we cannot be certain that any patent application will result in an issued patent or that our patents will not be circumvented, invalidated or declared unenforceable.

Our operating results and financial condition could be adversely affected if we become involved in intellectual property litigation. If we were to lose any such litigation, a court or a similar foreign governing body could invalidate or render unenforceable our owned or licensed patents, require us to pay significant damages, seek licenses and/or pay royalties to third parties, require us to redesign our products, or prevent us from manufacturing, using or selling our products, any of which would have an adverse effect on our results of operations and financial condition. The defense and prosecution of intellectual property suits and proceedings before the U.S. Patent and Trademark Office or its foreign equivalents are both costly and time consuming. Intellectual property litigation relating to our products could cause our customers or potential customers to defer or limit their purchase or use of the affected products until resolution of the litigation.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

**None**

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

**None**

**ITEM 4. SUBMISSIONS OF MATTERS TO A VOTE OF SECURITY HOLDERS**

**None**

**ITEM 5. OTHER INFORMATION**

**None**

**ITEM 6. EXHIBITS**

**None**