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AVIATION GENERAL INC
Form 10KSB
March 26, 2004

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-KSB

X ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2002

OR

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

Commission File Number: 0-24795

AVIATION GENERAL, INCORPORATED
(Exact name of registrant as specified in its charter)

Delaware (State of Incorporation) 73-1547645 (IRS Employer Identification No.)

7200 NW 63rd Street
Hangar 8, Wiley Post Airport
Bethany, Oklahoma 73008
(Address of principal executive offices) (Zip Code)

(405) 440-2255
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:
None

Securities registered pursuant to Section 12(g) of the Act:
Common stock; \$.50 par value

Indicate by check mark whether the registrant (1) has filed all reports 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 X No

Indicate by check mark if the disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this form 10-K. (X)

State issuer's revenue for its most recent fiscal year: \$2,142,000.

Based on the closing sales price of January 31, 2004 the aggregate market value of the voting stock held by non-affiliates of the registrant was \$650.

The number of shares outstanding of the registrant's common stock, \$.50 par value, was 8,270,397 at January 31, 2004.

Total number of pages including cover page 51.

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PART 1

Item 1. Business

Overview

Aviation General, Incorporated (the "Company" or "AGI") is a publicly traded holding company (Pink Sheets: AVGE.PK) incorporated under the laws of the State of Delaware. The Company has two wholly owned subsidiaries: Commander Aircraft Company ("CAC") and Strategic Jet Services, Inc. ("SJS"). Commander Aircraft Company (www.commanderair.com) manufactures, markets, and provides support services for its line of single engine, high performance Commander aircraft, and consulting, brokerage, and refurbishment services for all types of piston-powered aircraft. Strategic Jet Services, Inc. provides consulting, brokerage, sales, and refurbishment services for jet aircraft.

During the fourth quarter of 2002, SJS discontinued its operations, and CAC suspended indefinitely production of new aircraft. Other cost-cutting and overhead reductions were implemented due to the weakness in the Company's business. Management believes this weakness is primarily the result of depressed economic conditions and anxiety over terrorism and war in Iraq, which have had a pronounced, adverse effect on big-ticket, discretionary capital expenditures by businesses and individuals.

On December 27, 2002, Commander Aircraft Company filed a voluntary petition under Chapter 11 of the United States Bankruptcy Code for the District of Delaware. Commander Aircraft Company filed a final reorganization plan on July 5, 2003, following the execution of a letter agreement on that date with Tiger Aircraft, LLC. ("Tiger") to fund the plan. A stock purchase agreement was entered into with Tiger on November 1, 2003, pursuant to which an amended plan was filed on December 10, 2003. The U. S. bankruptcy court confirmed this plan on December 10, 2003, with the effective date scheduled for on or before March 31, 2004, unless extended by the consent of CAC, AGI, Tiger, the official committee of unsecured creditors, the U. S. Department of Labor, and Nyliak Investments, LLC.

The agreement with Tiger resulted from months of negotiations, contact with other potential investors, and legal proceedings pursuant to the bankruptcy process. Since the bankruptcy filing, Tiger has provided CAC with Debtor in Possession financing, which has allowed CAC to continue its operations and provide service and support to the fleet of Commander aircraft owners, refurbishment services, parts, and pre-owned aircraft brokerage. CAC expects to resume the production of new aircraft following the consummation of the transaction with Tiger.

Pursuant to the confirmed bankruptcy plan and agreement with Tiger, Tiger will invest approximately \$2.8 million in Aviation General, Incorporated in return for an 80% ownership interest in AGI. Approximately \$2 million will be used to settle with creditors in accordance with CAC's bankruptcy plan, and the remainder will be used for working capital. Pursuant to the agreement with Tiger, AGI must secure the approval of the agreement from its shareholders as well as their authorization to amend the Company's Certificate of Incorporation to increase the Company's authorized common shares from 20,000,000 shares to 100,000,000 shares. The Company currently has 20,000,000 common shares authorized and approximately 7,000,000 common shares (excluding Treasury stock which will be retired) issued and outstanding. The agreement with Tiger will necessitate the issuance of approximately 28,000,000 new shares of common stock

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to Tiger, resulting in a total of approximately 35,000,000 shares to be issued and outstanding.

Forward Looking Statements

This form 10-KSB includes certain statements that may be deemed to be "forward-looking statements" within the meaning of Section 27A of the Securities Act. All statements, other than statements of historical fact, included in this Form 10-KSB that address activities, events or developments that the Company expects, projects, believes, or anticipates will or may occur in the future,

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including matters having to do with CAC's emergence from bankruptcy and continuance as a going concern, expected and future aircraft sales and service revenues, CAC's ability to fund its operations and repay debt, business strategies, expansion and growth of operations and other such matters, are forward-looking statements. These statements are based on certain assumptions and analyses made by our management in light of its experience and its perception of historical trends, current conditions, expected future developments, and other factors it believes are appropriate in the circumstances. These statements are subject to a number of assumptions, risks and uncertainties, including general economic and business conditions, the business opportunities (or lack thereof) that may be presented to and pursued by the Company and its performance with respect to contracts and its success in developing new business, the ability to attract and retain qualified employees, and other factors, many of which are beyond the Company's control. You are cautioned that these forward-looking statements are not guarantees of future performance and that actual results or developments may differ materially from those projected in such statements.

History

Commander Aircraft Company was incorporated in 1988 upon the acquisition from Gulfstream Aerospace Corporation of the Commander single engine product line. The original Commander single engine aircraft was designed and manufactured by Rockwell International Corporation and received certification from the Federal Aviation Administration ("FAA") in 1972. Between 1972 and 1979, Rockwell produced 1,162 aircraft, including the Commander 112, 112TC, 114, and other models. Rockwell ceased production in 1979 and sold its General Aviation Division to Gulfstream Aerospace Corporation in 1981. Gulfstream never manufactured Commander single engine aircraft.

After CAC acquired the Commander single engine product line in 1988, it designed, engineered and implemented significant improvements to the proven Rockwell Commander line, resulting in the new CAC Commander 114B. CAC was issued a new Type Certificate for the Commander 114B by the FAA in 1992 and commenced production. The 114B features include an extensive range of avionics equipment, retractable landing gear, a 260 horsepower fuel-injected engine, a constant speed propeller, a standard range of 725 nautical miles (833 statute miles), a 1,216 pound useful load, a maximum cruise speed of 164 knots (188 miles per hour), a large luxurious four-place cabin, and low operating and maintenance costs.

In 1994, CAC added the Commander 114AT All-Purpose Trainer to its line of single engine, high performance aircraft. The Commander 114AT is a four-place high performance trainer designed for military, professional, and civilian flight training. An all-in-one aircraft, the Commander 114AT All-Purpose Trainer is ideal for primary through instrument flight training. The Commander 114AT

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shares the same design heritage as the luxurious Commander 114B, with a modified instrument panel and more utilitarian interior.

In 1995, CAC received certification from the FAA for the Commander 114TC, a turbocharged version of the Commander 114B. The Commander 114TC is equipped with the same expansive interior and state-of-the-art systems as the Commander 114B, but utilizes a 270 horsepower turbocharged Lycoming engine, which provides speeds up to 197 knots (227 miles per hour). The Commander 114TC is certified to an altitude of 25,000 feet, which makes it an excellent aircraft for mountainous regions, as well as high-density altitude environments. Like the 114B, the Commander 114TC has received numerous favorable reviews by the aviation press.

In 2000, CAC introduced the 115 series of high performance, single engine aircraft. The Commander 115 and 115TC represent the culmination of a variety of improvements to the Commander line, and feature numerous airframe, engine and systems refinements, as well as significantly increased range capability and an upgraded avionics package which includes global navigation, communication, and

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moving map displays. The Commander 115 series is the latest of a thoroughbred line of aircraft that offer a combination of performance, comfort, safety, and utility.

To date, approximately \$50 million has been invested to build Commander Aircraft Company. In an industry where a \$100 million investment is often insufficient to engineer, design, and FAA type certify an aircraft, management believes that CAC's achievements are considerable. They include: the acquisition of Rockwell's single engine high performance Commander aircraft line, the modification and enhancement of the value of the existing fleet of Commander aircraft built from 1972 through 1979 by Rockwell International Corporation, extensively enhancing the aerodynamics, avionics, systems, interior, and power plant of the original Rockwell Commander design resulting in a new aircraft FAA type certification designated 114B and 114TC, the introduction of new avionics packages, enhancements and derivative aircraft models (the current 115 and 115TC series), and the establishment of manufacturing operations and marketing, aircraft brokerage, refurbishment, and service and support capabilities.

CAC is one of the few companies in the world with an FAA Type Certificate for production of a four-place single engine high performance aircraft. Commander aircraft are certified to the more recent stringent standards of FAR 23 through Amendment 7 and have had zero airframe ADs (Airworthiness Directives) since re-certification in 1992. Management believes that Commander aircraft have a strong reputation in their class due to their superior safety, design, quality, comfort, reliability, resale value, and ramp appeal.

Industry Overview

The general aviation industry originated in the United States in 1903 with the first flight of an aircraft by the Wright brothers. Today, general aviation is a multi-billion dollar international industry, which includes the production, sale and servicing of non-military and non-commercial single engine piston, multi engine piston, turboprop, and turbojet aircraft. The U. S. general aviation industry is uniquely American and considered the best in the world.

There are approximately 155,000 previously produced single engine piston aircraft in the United States that are still flying today, of which approximately one-third, or 50,000, aircraft are single engine high performance aircraft. The average age of the single engine high performance fleet is approximately 35 years, and the Company estimates that the replacement value of

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these aircraft is over \$15 billion.

Although the general aviation market has been depressed in recent years, we believe that the market for single engine high performance aircraft could improve as a result of: an improving economy, attrition of the aging fleet of aircraft, evolution of new international markets for general aviation aircraft, increased use of single engine aircraft as a corporate tool for small and medium sized businesses, and demand for advances single engine trainers.

The market for pre-owned general aviation aircraft, from single engine to jet aircraft, is substantially larger than the market for new aircraft as are the attendant markets for pre-owned aircraft refurbishment, avionics, and service and support.

According to the General Aviation Manufacturers Association ("GAMA"), general aviation ("GA") is one of our nation's most important and dynamic industries, flying over 32 million hours (nearly twice the major airlines' flight hours) and carrying 166 million passengers annually. GA is relied on exclusively by more than 5,400 communities as their only source of air transportation, (scheduled airlines serve approximately 600 of 5,400 airports). Approximately 70 percent of the hours flown by GA are for business and commercial purposes.

- GA aircraft range from two-seat training aircraft to intercontinental business jets.

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- GA is estimated to be an \$18 billion industry.
- Domestic GA exports one-third of its production and leads the world in development of new technology aircraft.
- Most people first learn to fly in a GA aircraft.

There are approximately 219,464 active GA and air taxi aircraft in the USA (excluding commuters). Of this total, more than half (150,886) are single-engine piston aircraft. GA enjoys the use of over 5,000 airports in the United States.

Business Strategy

Commander Aircraft Company has established a business model that management believes distinguishes it from its competitors. CAC has a low volume, high margin, diversified revenue and value-added service base model rather than a high volume, low margin, pure manufacturing model. Depending upon contributions from CAC's non-manufacturing activities, CAC believes it can achieve break-even financial results with the manufacture and sale of as few as 12 to 15 new Commander aircraft per annum and could achieve significant profitability above these levels.

CAC's model is built on the following foundation:

- Manufacture, service, and support of high-end aircraft with a reputation for high quality.
- Assembly-manufacturer operations allow streamlined production, lower capital investment in equipment, smaller production staff and size of manufacturing facility.
- Semi-custom built to order in accordance with customer specifications of avionics, equipment, paint, and interior with customer deposits upon order and progress payments during the manufacturing process.
- Factory direct sales in the U. S. (instead of using dealers, which receive a 15-25% discount).

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- Appointment of leading aviation fixed-based operators ("FBOs") as Commander Authorized Service Centers as referral sources for new aircraft orders and ability to provide complementary service and support functions.
- Diversification into pre-owned piston aircraft brokerage, refurbishment services, paint, part, and avionics - encouraging our customers to deal directly with the factory whenever possible.

This strategy served CAC well with revenues doubling from approximately \$8.0 million in 1997 to \$16.8 million in 2000 and the achievement of profitability. Based on trends of the previous years and sales and marketing forecasts, CAC significantly increased its production schedule for 2001 and had to scale it back as the economy, particularly manufacturing, began to slide into a prolonged recession. The depressed domestic and international economic climate, which is continuing, has been coupled with one of the largest declines in history of asset values in the U. S. securities markets, terrorist attacks, and the uncertainty over the international situation and war with Iraq.

During 2001 and 2002, CAC's marketing, sales, and advertising expenditures declined significantly due to budget constraints, and as a result CAC incurred several significant financial charges.

Notwithstanding the disappointing financial results of the last two years and subsequent bankruptcy filing and suspension of new aircraft production, CAC believes its business model is sound and that, with adequate capitalization and emergence from bankruptcy, CAC can return to profitability in the future following the recommencement of new aircraft production and funding for appropriate marketing, sales, and advertising.

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Marketing Strategy

There are an estimated 55,000 general aviation single engine high performance aircraft in existence (approximately one-third of the total single engine fleet). The average age of these aircraft is over 35 years, and the Company estimates that the cost of replacing the fleet of such aircraft would exceed \$15 billion. CAC is one of the few companies in the world with an FAA Type Certificate for production of a four-place single engine high performance aircraft. Commander aircraft are certified to the more recent stringent standards of FAR 23 through Amendment 7 and have had zero airframe ADs since re-certification in 1992.

CAC believes its aircraft possess many qualities superior to those of its competitors including safety, design, comfort, performance, quality, resale value, utility, and ramp appeal. Furthermore, CAC offers value-added services and programs such as a turn-key ownership program, certified flight instructor program, and trade-up program together with assistance with financing, insurance, trade-ins, training, hangaring, and pilot services.

Commander Aircraft Company believes the market for its products will improve as a result of attrition of the existing fleet of aging single engine, high performance aircraft, development of new international markets for general aviation aircraft, and increased use of single engine aircraft as a cost/convenience effective corporate tool for small and medium sized businesses.

CAC's primary targeted markets are as follows:

- The existing pilot base comprised of pilots who may or may not currently own aircraft.

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- New pilots in various stages of pilot training.
- Small and medium sized businesses with regional travel needs.

To address these markets, CAC has developed:

- The Commander Trade-Up Program, which targets owners of other aircraft types.
- The Commander CFI Program, which targets newer pilots and their Certified Flight Instructors by bringing both together in the aircraft evaluation and acquisition process.
- The Commander Aircraft Ownership Program, which provides business owners who may be non-pilots with a complete turn-key program including aircraft acquisition, financing, insurance, maintenance, storage, product support, private pilot service, and instruction, if desired.

CAC stresses the superior aspects of its aircraft such as safety, design, quality, comfort, reliability, resale value, and ramp appeal as well as value-added service and support through direct contact and growing relationships with its prospects and customers.

CAC implements its marketing strategy via factory direct sales comprised of regional sales personnel who are directly managed and supported from CAC's headquarters in Oklahoma. The marketing organization is augmented by a worldwide network of Commander Authorized Service Centers (ASCs), which are leading independent FBOs (fixed base operators). CAC believes that factory direct sales and marketing of its products and services provides total control of product pricing, quality, and business integrity in addition to unsurpassed customer relations and repeat business. Unfortunately, CAC's marketing, sales, and advertising expenditures have been sharply curtailed over the past two years due to budget constraints.

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Competition

Commander Aircraft Company competes in the single engine high performance category directly with normally aspirated and turbo-charged aircraft of the same type produced by Raytheon's Beechcraft unit, the New Piper Aircraft Company, Mooney Aerospace Group, and Aerospatiale's Socata subsidiary. CAC also competes, for aircraft purchasers, indirectly with aircraft in other categories such as: single engine fixed gear aircraft manufactured by Cessna, Cirrus, and Lancair, single engine pressurized and turboprop aircraft, twin engine aircraft and alternatives available to purchasers in the pre-owned market.

Purchasers of single engine, high performance aircraft choose among competitive models on the basis of numerous factors, including performance, reliability, price, appearance, quality of service and reputation of the aircraft and the manufacturer. Commander Aircraft Company believes that it can favorably compete with its competitors on the basis of the safety, quality, comfort, and performance of its aircraft, and the quality and scope of the support services CAC provides to its customers. CAC further believes its aircraft are competitively priced and have a number of features, including certification to stricter standards, newer, more attractive design and larger cabin size, which make them competitive with or superior to the single engine, high performance aircraft produced by its four principal competitors. Raytheon Aircraft Corporation suspended production of one of its single engine, high performance models, the F33A Bonanza, in 1994. Raytheon's other single engine, high performance model, the A36, remains in production. However, it is decades older in design, FAA certified to lesser standards, and has an inferior safety record

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than Commander aircraft. Mooney Aerospace Group produces single engine, high performance aircraft that are significantly smaller than the Commander 115 and 115TC, and Mooney aircraft are also decades older in design and FAA certified to lesser standards with inferior safety records. New Piper Aircraft Corporation produces a single engine, high performance, six place aircraft with similar performance, the normally aspirated and turbo-charged Saratoga/Cherokee series, which again is decades older in design, FAA certified to lesser standards, and possesses a substantially inferior safety record to Commander aircraft. Socata's marketing efforts are, for the most part, focused in Europe and Asia. Each of these competitors has been well established in the general aviation industry for years and may have access to greater resources than are available to CAC.

Commander Aircraft Company's aircraft are decades newer in design than the Bonanza, Mooney and Piper competitive models and are certified to the newer, more stringent Federal Aviation Administration ("FAA") Regulation (FAR) 23 through Amendment 7 standard rather than the older Civil Air Regulation (CAR) 3. The Commander line has the best safety record in its class, according to an independent study of FAA and National Transportation and Safety Board ("NTSB") statistics conducted by R. E. Breiling Associates, the leading accident analysis firm in general aviation.

Factors inhibiting our market share include:

- Our competitors' larger outstanding fleets of aircraft, which are eight to ten times the size of ours, providing them with a larger pool of potential trade-in business.
- Our competitors' use of dealers.
- Our competitors' significantly greater expenditures on marketing and advertising.
- Our competitors' pricing policies.

Commander Aircraft Company believes its aircraft are superior in many respects, including safety, design, quality, comfort, reliability, resale value, and ramp appeal, and accordingly, Commander aircraft are priced approximately 10-25% higher than those of our competitors, except for the Beech Bonanza series, which

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are priced approximately 10-20% higher than comparably equipped Commander aircraft. Inherent in our pricing are value-added programs, and individual consultation with each purchaser and customization of each aircraft in accordance with their specifications.

Unfortunately, economic conditions during the past several years have caused price deflation in manufactured goods, with aircraft among the most affected products. Our competitors have been unable to maintain pricing integrity and have resorted in many cases to price reduction policies intended to foster sales. We believe that these competitors will not be able to sustain these policies as the margins they result in are not profitable. Although our competitors have reduced prices, we plan to maintain our prices while offering additional avionics as standard equipment on our aircraft, making it more price competitive with comparably equipped aircraft offered by our competitors.

Insurance

Commander Aircraft Company normally carries most types of insurance customary for a manufacturer of general aviation aircraft, including coverage for general liability, property damage, aircraft loss or damage and worker's compensation,

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but does not carry product liability insurance. At December 31, 2002, all insurance coverage had been suspended due to the inability of the Company to pay for this coverage. There is no assurance that the amount of insurance carried by CAC would be sufficient to protect it fully in the event of a serious accident and liability claim, but CAC believes that the amounts and coverage of its insurance protection are reasonable and appropriate for the CAC's business operations. Although highly probable, there is no assurance that such insurance will continue to be available on commercially reasonable terms.

From time to time, Commander Aircraft is the target of litigation, including suits filed regarding accidents of Commander aircraft. In mid 1994, Congress enacted the General Aviation Revitalization Act, S. 1458 ("GARA"), which established an 18-year statute of repose for general aviation aircraft and component manufacturers. GARA prohibits product liability suits against aircraft manufacturers for aircraft that are more than 18 years old when an accident occurs. This action eliminated from the liability tail all Rockwell-manufactured Commander aircraft, last produced in 1979. The only aircraft for which the Company has potential liability as a manufacturer are aircraft it has produced since 1992. This currently represents approximately 200 aircraft, approximately 70 of which have been exported outside of the United States.

Through March 1, 1995, CAC maintained product liability insurance with coverage of \$10 million per occurrence and \$10 million in the aggregate, with deductible of \$200,000 for aircraft built through March 1, 1995. Management believes that the premiums for this type of insurance are rapacious, the policies are full of holes, the insurance companies end up controlling any litigation and are loathe to vigorously defend unwarranted claims, and prefer to settle and raise premiums rather than defend unwarranted claims. Thus, management believes that the interest of shareholders is better served by vigorously defending claims through the services of highly qualified specialists and attorneys rather than retaining product liability insurance to settle exorbitant claims. As such, CAC elected not to retain product liability insurance coverage commencing March 1, 1995. CAC could be exposed to significant financial risks if losses from product liability were to occur. Since CAC dropped its product liability insurance in 1995, it has saved an estimated \$8-10 million in insurance premium costs versus expenditures of approximately \$1.5 million in litigation and settlement costs, most of which would have been expended even with liability insurance because of insurance policy deductibles.

The General Aviation Revitalization Act established an 18-year statute of repose for general aviation aircraft and component manufacturers. This law prohibits product liability suits against aircraft manufacturers when the aircraft involved in an accident is more than 18 years old when the accident occurs. This

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action eliminated all Rockwell manufactured Commanders produced in the 1970's from CAC's liability tail. The only aircraft that CAC bears manufacturing responsibility for are the models 115, 115TC, 114B, 114TC, and 114AT produced from 1992 through the present, which currently represent approximately 200 aircraft.

Parts and Materials Availability

Commander Aircraft Company purchases parts and materials from over 100 different suppliers. Though some of these vendors are key to the manufacture of CAC's aircraft, there are no long-term commitments or contracts with any suppliers. CAC considers its relationship with its suppliers, including those affected by the bankruptcy filing, to be satisfactory and does not anticipate any shortages or interruption to production due to lack of available components on a timely

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basis.

Government Regulations

In order for an aircraft model to be manufactured for sale, the FAA must issue a Type Certificate for the aircraft model and, in order for a particular aircraft to be operated, an Airworthiness Certificate for that aircraft must be issued. Commander Aircraft Company was issued a Type Certificate for the Commander 114B in 1992 and a Type Certificate for the Commander 114TC in 1995. CAC owns Type Certificates for all predecessor and current single engine Commander models. The sale of CAC's product internationally is subject to regulation by comparable agencies in foreign countries.

CAC received a Production Certificate from the FAA in 1993, which allows CAC to issue Airworthiness Certificates from the FAA. An Airworthiness Certificate is issued for a particular aircraft when it is certified to have been built in accordance with specifications approved under the Type Certificate for that particular model aircraft. Commander aircraft are certified to FAR 23, Amendment 7, meeting more stringent standards for single engine aircraft than aircraft certified under the older CAR 3 regulations. CAC's production certificate has remained dormant during suspension of new aircraft production. CAC plans to reactivate its production certificate upon recommencing new aircraft production. Although a production certificate is not necessary to produce aircraft, having one facilitates the production process and interaction with the FAA.

Employees

The Company has a total of 14 full-time and 3 contract employees as of January 21, 2004. The Company believes that its future success will depend, in part, upon its continued ability to recruit and retain highly skilled employees. Although competition for qualified personnel is strong, the Company has been successful in attracting and retaining skilled employees. None of the Company's employees are covered by a collective bargaining agreement, and the Company considers its employee relations to be good. The Company believes resumption of new aircraft production and achievement of profitable financial results will require approximately 50 to 60 full-time employees.

Item 2. Properties

The Company has operated in a 103,650 square foot facility, which consists of three buildings constructed in 1981, located at the Wiley Post Airport in Bethany, Oklahoma. The Company performs all of its operations and services from this facility. During the past ten years, the Company has improved its facility to assure safety and compliance with environmental laws and regulations.

In 2003, the Company transferred its lease with the Oklahoma City Airport Trust Authority to The Servicer, Inc., a company with plans to operate a Fixed Base Operation in the facility and to provide significant aesthetic upgrades to the facility. The Company negotiated a 3.5 year sub-lease for 50,011 square feet of manufacturing, service and office space, guaranteed renewable at six-month intervals.

A summary of lease payments is presented in Note G - Leases, of the Notes to Consolidated Financial Statements for 2002.

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Item 3. Legal Proceedings

The Company is a defendant in a lawsuit resulting from a crash of one its manufactured aircraft. Management does not believe the Company bears any responsibility and has vigorously defended against this claim. The National Transportation and Safety Board accident investigation has found the probable cause of this crash was pilot error. This matter will be discharged pursuant to the bankruptcy plan upon its completion. The Company is also a defendant resulting from a crash of a 1977 Rockwell Commander aircraft that was not manufactured by the Company and for which the Company believes it bears no responsibility, and in any event, will be discharged pursuant to the bankruptcy plan upon its completion.

On December 27, 2002, CAC filed a voluntary petition under Chapter 11 of the United States Bankruptcy Code in the United States bankruptcy court for the District of Delaware. CAC filed a final reorganization plan on July 5, 2002, following the execution of a letter of agreement on that date with Tiger Aircraft, LLC ("Tiger") to fund the plan. A stock purchase agreement was entered into with Tiger on November 1, 2003, pursuant to which an amended plan was filed on December 10, 2003, with the effective date scheduled for on or before March 31, 2004, unless extended by the consent of CAC, AGI, Tiger, the official committee of unsecured creditors, the U.S. Department of Labor, and Nyliak Investments, LLC. For additional information, see Note R of Notes to Consolidated Financial Statements.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year covered by this report.

PART II

Item 5. Market for the Registrant's Common Stock and Related Shareholder

Matters

The common stock of Aviation General, Incorporated, \$.50 par value (symbol AVGE.PK), trades on the NASDAQ Small-Cap Market until it was delisted and began trading on the over-the-counter bulletin board on September 24, 2002 and has recently been traded on the pink sheets. This table presents its high and low market prices during the past two years. The Company has never paid dividends in the past, and does not intend to pay dividends in 2004.

| Quarter | Quarterly Common Stock Price Ranges | | | |
|---------|-------------------------------------|-----|------|-----|
| | 2002 | | 2001 | |
| | High | Low | High | Low |
| 1st | .38 | .23 | 1.75 | .81 |
| 2nd | .67 | .33 | 1.00 | .41 |
| 3rd | .95 | .28 | .70 | .20 |
| 4th | .30 | .05 | .42 | .20 |

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In 2002, The Company issued 251,516 shares of its common stock as settlement of certain obligations. Included were 136,364 shares issued for \$45,000 for Board of Directors fees and 115,152 shares issued for \$38,000 for sales commissions.

There were approximately 300 holders of record of the Company's common stock as of December 31, 2002.

Item 6. Selected Financial Data

The selected financial data presented below for each year in the five year period ended December 31, 2002 have been derived from the Company's audited

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financial statements. This data should be read in conjunction with the Financial Statements and related notes thereto and other financial information appearing elsewhere in this Form 10-K.

| | Year Ended December 31 | | | | |
|--|---|-----------|----------|----------|-----------|
| | (Amounts in thousands, except per share data) | | | | |
| | 2002 | 2001 | 2000 | 1999 | 1998 |
| Operation Data: | | | | | |
| ----- | | | | | |
| Net sales | \$ 8,443 | \$ 9,488 | \$16,831 | \$13,667 | \$10,712 |
| Net earnings (loss) | \$(4,285) | \$(5,520) | \$ 450 | \$ (385) | \$(1,849) |
| Earnings (loss) per share basic & diluted | \$ (.60) | \$ (.84) | \$ 0.07 | \$ (.05) | \$ (.25) |
| Balance Sheet Data: | | | | | |
| ----- | | | | | |
| Total assets | \$ 3,715 | \$ 7,304 | \$11,809 | \$ 8,632 | \$10,148 |
| Long-term debt | \$ 1,235 | \$ - | \$ - | \$ - | \$ - |

Item 7. Management's Discussion and Analysis of Financial Condition and Results

of Operations

You should read the following discussion and analysis together with our financial statements and accompanying notes appearing elsewhere in this Form 10KSB. The following information contains forward-looking statements that involve risks and uncertainties. Actual results may differ materially from those anticipated due to many factors, including those set forth under Items 1 and 3, Business and Legal Proceedings.

Critical Accounting Estimates and Accounting Policies

We must make estimates of the collectability of accounts receivable. We analyze historical write-offs, changes in our internal credit policies and customer concentrations when evaluating the adequacy of our allowance for doubtful accounts. Differences may result in the amount and timing of expenses for any period if we make different judgments or use difference estimates.

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Inventories are valued at the lower of cost or market. We must periodically evaluate the carrying value of our inventories to determine whether market conditions have impaired the carrying value of our inventories.

Property and equipment are evaluated for impairment whenever indicators of impairment exist. Accounting standards require that if an impairment indicator is present, the Company must assess whether the carrying amount of the asset is unrecoverable by estimating the sum of the future cash flows expected to result from the asset, undiscounted and without interest charges. If the carrying amount is less than the recoverable amount, an impairment charge must be recognized, based on the fair value of the asset. Management assumed the Company was a going concern for purposes of evaluating the possible impairment of its property and equipment. Should the Company not be able to continue as a going concern, there may be significant impairment in the value of the Company's property and equipment.

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We must estimate the future liability related to warranty work on new aircraft sold.

As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes. This process involves estimating our current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income, and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent that we establish a valuation allowance or increase this allowance in a period, we must include a tax provision or reduce our tax benefit in the statements of operations. We use our judgment to determine our provision or benefit for income taxes, deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets. We believe, based on a number of factors including historical operating losses, that we will not realize the future benefits of a significant portion of our net deferred tax assets and we have accordingly provided a full valuation allowance against our deferred tax assets. However, various factors may cause those assumptions to change in the near term.

We cannot predict what future laws and regulations might be passed that could have a material effect on our results of operations. We assess the impact of significant changes in laws and regulations on a regular basis and update the assumptions and estimates used to prepare our financial statements when we deem it necessary.

We have determined the significant principles by considering accounting policies that involve the most complex or subjective decisions or assessments. Our most significant accounting policies are those related to revenue recognition and accounting for stock-based compensation.

Aircraft Sales and Marketing

We recognize the sale of new aircraft when a purchase agreement is funded and title is transferred to the buyer, which occurs after the Company receives an airworthiness certificate from the Federal Aviation Administration. Sales of pre-owned aircraft are recognized upon execution and the funding of a purchase agreement. Service revenues are recognized when the services are performed.

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Our aircraft production is dependent upon the perception of our customers that the purchase of our aircraft is desirable over others that they could choose. Often the purchase of an aircraft is dependent upon investment decisions made by the buyer that could be affected by many factors. Among these factors are the general economic conditions at the time the decision is made, the performance of the buyer's investments and the tax treatment or possible changes in the tax treatment of the aircraft purchase for the buyer. Additionally, as we have seen in the last year, the perception of safety, both personal and national, can have an impact on the business of the Company.

Inventories

Our inventories, other than pre-owned aircraft, are stated at the lower of cost or market, and cost is determined by the average-cost method. The inventory costs include all direct manufacturing costs and overhead. The inventories consist of parts for manufacturing and servicing of aircraft, parts for resale and work in process, as well as new and pre-owned aircraft. Pre-owned aircraft are valued on a specific-identification basis at the lower of cost or current estimated realizable wholesale price.

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Results of Operations:

2002 vs. 2001

The Company's business began to rebound and improve in the first half of 2002 as compared to 2001. However, the economy entered into a renewed slowdown, which management believes was probably the result of continued weakness in the overall economy, which may have resulted from renewed anxiety over possible events such as anthrax, air travel, potential terrorist activities, and the march toward war with Iraq, and it caused a decline in the purchase of big-ticket durable goods such as automobiles and aircraft.

During the second half of 2002, the Company experienced cancellation or postponement of several new and pre-owned aircraft orders and transactions, causing a cash flow crisis resulting in the necessity of filing a Chapter 11 bankruptcy petition on December 27, 2002.

The Company, along with many other companies in the aviation industry, has been affected by macro political and economic events beyond its control and endeavored to adjust its new aircraft production schedule and overall business accordingly. However, there are lead and lag financial consequences to doing so. For example, the terrorist attacks on the United States in 2001, concurrent with the largest decline in asset values in the securities markets in history, and a weakening economy, presented enormous adjustment challenges to the Company.

The following is a more detailed explanation of the components of the financial results that were affected:

Revenues decreased 11% in 2002 to \$8,443,416 from \$9,487,795 in 2001, resulting in a net loss of \$(4,285,111) for 2002 compared to a net loss of \$(5,519,592) in 2001. The net loss per basic and diluted share was \$(0.60) in 2002 compared to a net loss of \$(0.84) per basic and diluted share in 2001.

Revenues from aircraft sales decreased 8% in 2002 to \$7,412,519 from \$8,027,663 in 2001. New aircraft deliveries were 6 units in 2002 compared to 8 units in 2001. Pre-owned and consigned aircraft sales decreased to 16 aircraft in 2002

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from 24 in 2001. Revenues generated by the service, parts and refurbishment business was \$1,030,897 in 2002 compared to \$1,460,132 in 2001.

Aircraft cost of sales was \$6,679,481 in 2002 as compared to \$7,665,233 for 2001. The gross margin on aircraft sales increased to 10% in 2002 from 5% in 2001.

Service and parts cost of sales was \$829,954 in 2002 compared to \$1,291,618 in 2001. The decrease was partially due to a lower volume of service activity and spare parts shipments, however, the gross margin on service and parts sales increased to 19% in 2002 from 12% in 2001.

Engineering and product development costs decreased to \$126,232 in 2002 from \$278,379 in 2001. The decrease in these expenses is due to the downsizing in this area.

Selling, general and administrative expenses decreased by 33% from \$3,616,933 in 2001 to \$2,440,414 in 2002. This decrease is due primarily to reductions both in the sales and administrative staffs and operations.

Also included in operating expenses for 2002 is an impairment of Work in Process (WIP), parts and aircraft inventory of \$1,758,620. Of this, pre-owned aircraft

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inventory was impaired by \$296,699 to reflect the depressed market values during the current recession, reducing the values to the lower of cost or market; WIP was impaired by \$510,506 in anticipation of the additional time and expenses necessary to restart manufacturing and; inventory was impaired by \$951,415 to reduce value of slow-moving inventories, thereby reducing the inventory values to the lower of cost or market. No such impairment was recognized in 2001.

During 2001, the Company recognized bad debts from a related party in the amount of \$1,529,889. There was no corresponding bad debts for 2002.

Interest income totaled \$1,929 in 2002, down from \$15,350 in 2001. This decrease was due to a reduction in interest bearing funds during 2002.

Interest expense decreased by 51% to \$243,414 in 2002 from \$498,715 in 2001 due to reduced activity in short-term borrowings from the Company's lines of credit.

Litigation settlements increased by 33% from \$150,000 in 2001 to \$200,000 in 2002. This increase was due to the settlement during 2002 of a claim resulting from a crash of a aircraft manufactured by the Company.

During 2002, the Company realized a loss on the sale of available for sale equity securities in the amount of \$(395,973)

Liquidity and Capital Resources

Cash used in operations totaled \$(648,036) for 2002 compared to cash provided by operations of \$868,244 in 2001.

Inventories decreased by \$2,927,701 primarily due in part to the recognition of \$1,758,620 in impairments on inventory and in part due to the reduction in the number of new and used aircraft held in inventory.

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Accounts payable decreased by \$163,229 at December 31, 2002. Long-term debt increased to \$1,234,795. The Company had no long-term debt as of December 31, 2001 and 2000.

The Company had no capital expenditures in 2002.

The Company established a line of credit with a bank in the amount of \$2,500,000 for the purpose of funding pre-owned aircraft for inventory. The notes bear interest at prime plus 1% and are secured by individual aircraft and certain guarantees. In addition, the Company established a line of credit with a financial institution in the amount of \$3,000,000 to provide funding for new aircraft as well as pre-owned piston and turbine aircraft. The notes contain variable interest rates up to 12.5%, mature in six-month intervals and are renewable at the option of the Company for an additional six months. Borrowings under these lines of credit totaled \$1,359,819 at December 31, 2002.

For 2002, the Company reported \$8,443,416 in revenues and a loss, \$(4,285,111), with six new aircraft deliveries. For the year 2001, the Company reported \$9,487,795 in revenues and a loss of \$(5,519,592), with deliveries of eight new aircraft.

Contractual Obligations and Commercial Commitments. The following table is a summary of the Company's contractual obligations as of December 31, 2002.

| | Payment Due by Period | | | |
|----------------------|-----------------------|-----------------------|-------------|------------|
| | Total | Less than One Year | 1-3 Years | Thereafter |
| | ----- | ----- | ----- | ----- |
| Long-Term Debt | \$1,234,795 | \$ - | \$1,234,795 | \$ - |
| Current Note Payable | 1,359,819 | 1,359,819 | - | - |
| Operating Leases | 396,900 | 75,600 | 226,800 | 94,500 |
| | ----- | ----- | ----- | ----- |
| Total | \$2,991,514 | \$1,435,419 | \$1,461,595 | \$ 94,500 |
| | ===== | ===== | ===== | ===== |

As we go forward in 2004, management believes that economic conditions and financial markets appear to have stabilized and that the Company could benefit from increased interest in general aviation, due to inconvenience and safety factors now attendant with commercial airline travel. The Company could also benefit from historically low interest rates, which lower significantly the financing cost of aircraft purchases.

Market Risk

The Company's market risk is impacted by changes in interest rates, foreign currency exchange rates and certain equity security prices. The note receivable held by the Company includes a quarterly adjustment clause, which permits the Company to increase or decrease, the amount of interest charged based on bank prime rates. All transactions with international customers are made in U.S. dollars, thereby minimizing the risk associated with foreign currency exchange

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rates. The Company's investment in equity securities is classified as available-for-sale with unrealized gains or losses excluded from income and reported as other comprehensive income. The Company has no significant risk associated with commodity prices.

Inflation -----

Management believes that the overall effects of inflation on the Company's costs of materials and supplies have been minimal. For each of the past five years, cost of sales was virtually the same as it would have been on a current cost basis. The Company uses a moving average cost for inventory valuation and cost changes are not readily recognized in the short-term.

Item 8. Financial Statements and Supplementary Data -----

Index to Financial Statements and Supplementary Data:

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| Financial Statements: | |
| Consolidated Balance Sheet December 31, 2002 | 21 |
| Consolidated Statements of Operations for the years ended December 31, 2002 and 2001 | 23 |
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| Consolidated Statements of Cash Flows for the years ended December 31, 2002 and 2001 | 25 |
| Notes to Consolidated Financial Statements | 27 |

Report of Independent Certified Public Accountants

Board of Directors and Stockholders
Aviation General, Incorporated

We have audited the accompanying consolidated balance sheet of Aviation General, Incorporated and Subsidiaries as of December 31, 2002, and the related consolidated statements of operations, stockholders' equity, and cash flows for the years ended December 31, 2002 and 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial

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statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Aviation General, Incorporated and Subsidiaries as of December 31, 2002, and the results of their operations and their cash flows for the years ended December 31, 2002 and 2001 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Notes A and Q to the consolidated financial statements, the Company has suffered recurring losses from operations that raise substantial doubt about its ability to continue as a going concern. Management's plans in regard to these matters are also described in Note Q. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

\s\Murrell, Hall, McIntosh & Co., PLLP
Murrell, Hall, McIntosh & Co., PLLP

Oklahoma City, Oklahoma
January 30, 2004

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AVIATION GENERAL, INCORPORATED AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2002

ASSETS

CURRENT ASSETS:

| | |
|-----------------------------------|-----------|
| Accounts receivable | \$ 9,431 |
| Inventories | 3,211,531 |
| Prepaid expenses and other assets | 3,591 |
| | ----- |
| Total current assets | 3,224,553 |
| | ----- |

PROPERTY AND EQUIPMENT - AT COST:

| | |
|--------------------------------|-------------|
| Office equipment and furniture | 365,373 |
| Vehicles and aircraft | 95,115 |
| Manufacturing equipment | 385,179 |
| Tooling | 676,747 |
| Leasehold improvements | 112,748 |
| | ----- |
| | 1,635,162 |
| Less accumulated depreciation | (1,144,693) |
| | ----- |
| | 490,469 |
| | ----- |

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\$ 3,715,022

=====

The accompany notes are an integral part of these financial statements.

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AVIATION GENERAL, INCORPORATED AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

DECEMBER 31, 2002

LIABILITIES AND STOCKHOLDERS' EQUITY

CURRENT LIABILITIES:

LIABILITIES NOT SUBJECT TO COMPROMISE -

| | |
|---------------------------|-----------|
| Cash overdraft | \$ 2,145 |
| Notes payable | 1,359,819 |
| | ----- |
| Total current liabilities | 1,361,964 |

LIABILITIES SUBJECT TO COMPROMISE -

| | |
|---|-----------|
| Accounts payable | 2,146,221 |
| Accrued expenses | 1,299,117 |
| Refundable deposits | 146,500 |
| | ----- |
| Total liabilities subject to compromise | 3,591,838 |
| | ----- |

| | |
|---------------------------|-----------|
| Total current liabilities | 4,953,802 |
| | ----- |

NONCURRENT LIABILITIES:

| | |
|---------------|-----------|
| Notes payable | 1,234,795 |
| | ----- |

REDEEMABLE COMMON STOCK - \$.01 par value; issued, 150,000 shares in 2001; stated at redemption value

| |
|---------|
| 150,000 |
| ----- |

STOCKHOLDERS' EQUITY (DEFICIT):

| | |
|---|--------------|
| Preferred stock - \$.01 par value; 5,000,000 authorized shares; no shares outstanding | - |
| Common stock, \$.50 par value; 20,000,000 shares authorized; 8,120,397 at December 31, 2002 | 4,060,198 |
| Additional paid-in capital | 37,254,305 |
| Less: Treasury stock at cost, 1,009,551 shares at December 31, 2002 | (1,709,638) |
| Accumulated (deficit) | (42,228,440) |
| Accumulated other comprehensive income (loss) | - |
| | ----- |
| Total stockholders' equity (deficit) | (2,623,575) |
| | ----- |

\$ 3,715,022

=====

The accompany notes are an integral part of these financial statements

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AVIATION GENERAL, INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 2002 AND 2001

| | 2002 | 2001 |
|--|--------------|--------------|
| | ----- | ----- |
| NET SALES: | | |
| Aircraft | \$ 7,412,519 | \$ 8,027,663 |
| Service | 1,030,897 | 1,460,132 |
| | ----- | ----- |
| | 8,443,416 | 9,487,795 |
| | ----- | ----- |
| COST OF SALES: | | |
| Aircraft | 6,679,481 | 7,665,233 |
| Service | 829,954 | 1,291,618 |
| | ----- | ----- |
| | 7,509,435 | 8,956,851 |
| | ----- | ----- |
| Gross margin | 933,981 | 530,944 |
| | ----- | ----- |
| OTHER OPERATING EXPENSES: | | |
| Product development and engineering costs | 126,232 | 278,379 |
| Selling, general, and administrative expenses | 2,440,414 | 3,616,933 |
| Impairments and allowances | 1,758,620 | - |
| Bad debt expense - related party | - | 1,529,889 |
| | ----- | ----- |
| Total operating expenses | 4,325,266 | 5,425,201 |
| | ----- | ----- |
| Operating income (loss) | (3,391,285) | (4,894,257) |
| | ----- | ----- |
| OTHER INCOME (EXPENSES): | | |
| Interest income | 1,929 | 15,350 |
| Other income | 27,564 | 23,770 |
| Interest expense | (243,414) | (498,715) |
| Other expense | (65,966) | (15,740) |
| Litigation settlement | (200,000) | (150,000) |
| Loss abandonment of lease | (17,966) | - |
| Realized loss on available for sale equity securities | (395,973) | - |
| | ----- | ----- |
| Total other expenses | (893,826) | (625,335) |

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| | | |
|---|----------------|----------------|
| NET (LOSS) | \$ (4,285,111) | \$ (5,519,592) |
| NET (LOSS) PER SHARE | | |
| Weighted average common shares outstanding; basic | 7,143,250 | 6,581,467 |
| Net (loss) per share; basic | \$ (.60) | \$ (.84) |
| Weighted average common shares outstanding; diluted | 7,143,250 | 6,581,467 |
| Net (loss) per share; diluted | \$ (.60) | \$ (.84) |

The accompany notes are an integral part of these financial statements

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AVIATION GENERAL, INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

YEARS ENDED DECEMBER 31, 2002 AND 2001

| | Common Stock Shares | Common Stock Amount | Additional Paid-in Capital | Treasury Stock Shares | Treasury Stock Amount | Accumulated Deficit |
|--|------------------------|------------------------|----------------------------------|--------------------------|--------------------------|------------------------|
| Balance at | | | | | | |
| January 1, 2001 | 7,051,519 | \$ 3,525,759 | \$ 36,889,799 | 772,189 | \$ (1,294,193) | \$ (32,423,7 |
| Issuance of common stock | 580,000 | 290,000 | 110,500 | - | - | |
| Comprehensive income: | | | | | | |
| Net loss | - | - | - | - | - | (5,519,5 |
| Other comprehensive loss - | | | | | | |
| Change in unrealized investment gain, net | - | - | - | - | - | |
| Comprehensive income | - | - | - | - | - | (5,519,5 |

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| | | | | | | | |
|---------------------|-----------|------------|--------------|-------------|----------------|--------------|-------|
| Balance at | | | | | | | |
| December 31, 2001 | 7,631,519 | 3,815,759 | 37,000,299 | 772,189 | (1,294,193) | (37,943,3 | |
| Treasury Stock not | | | | | | | |
| retired as planned | 237,362 | 118,681 | 296,764 | 237,362 | (415,445) | | |
| Issuance of | | | | | | | |
| common stock | 251,516 | 125,758 | (42,758) | - | - | | |
| Comprehensive loss: | | | | | | | |
| Net loss | - | - | - | - | - | (4,285,1 | |
| Other comprehensive | | | | | | | |
| income - | | | | | | | |
| Change in | | | | | | | |
| unrealized | | | | | | | |
| investment | | | | | | | |
| loss, net | - | - | - | - | - | | |
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| Comprehensive | | | | | | | |
| loss | - | - | - | - | - | (4,285,1 | |
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| Balance at | | | | | | | |
| December 31, 2002 | 8,120,397 | \$4,060,19 | \$37,254,305 | \$1,009,551 | \$ (1,709,638) | \$ (42,228,4 | |
| | ===== | ===== | ===== | ===== | ===== | ===== | ===== |

The accompany notes are an integral part of these financial statements

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AVIATION GENERAL, INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2002 AND 2001

| | 2002 | 2001 |
|---------------------------------------|---------------|---------------|
| | ----- | ----- |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net (loss) | \$(4,285,111) | \$(5,519,592) |
| Adjustments to reconcile net | | |
| earnings (loss) to net cash provided | | |
| by (used in) operating activities | | |
| Depreciation and amortization | 130,684 | 120,098 |
| Common stock issued for litigation | | |
| settlement, services, and interest | | |
| charges | 83,000 | 450,500 |
| Receipts on aircraft notes receivable | 101,896 | 19,653 |
| Bad debt expense - related party | - | 1,529,889 |
| Loss on retirement of | | |
| property and equipment | 17,965 | - |
| Realized loss on sale of | | |
| available-for-sale equity | | |
| securities | 395,973 | 14,508 |
| Changes in assets and | | |

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| | | |
|---|-------------|-------------|
| liabilities: | | |
| (Increase) decrease in - | | |
| Accounts receivable | (9,431) | 551,425 |
| Inventories | 2,927,701 | 1,852,939 |
| Prepaid expenses and other - assets | 66,564 | 83,335 |
| Increase (decrease) in | | |
| Accounts payable | (163,229) | 1,083,036 |
| Accrued expenses | 685,001 | 52,718 |
| Refundable deposits | (599,049) | 629,735 |
| | ----- | ----- |
| Net cash provided by (used in) operating activities | (648,036) | 868,244 |
| | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Capital expenditures | - | (37,243) |
| Proceeds from available-for-sale equity securities | - | 20,260 |
| | ----- | ----- |
| Net cash provided by (used in) investing activities | - | (16,983) |
| | ----- | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from borrowings | 3,693,325 | 4,486,810 |
| Payments on borrowings | (3,258,790) | (5,261,731) |
| | ----- | ----- |
| Net cash provided by (used in) financing activities | 434,535 | (774,921) |
| | ----- | ----- |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (213,501) | 76,340 |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | 211,356 | 135,016 |
| | ----- | ----- |
| CASH AND CASH EQUIVALENTS (OVERDRAFT) AT END OF YEAR | \$ (2,145) | \$ 211,356 |
| | ===== | ===== |

The accompany notes are an integral part of these financial statements

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AVIATION GENERAL, INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED

YEARS ENDED DECEMBER 31, 2002 AND 2001

| | | |
|--|-------|-------|
| | 2002 | 2001 |
| | ----- | ----- |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION: | | |
| Cash paid during the year for - | | |

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| | | |
|--------------|------------|------------|
| Interest | \$ 260,928 | \$ 493,000 |
| Income taxes | - | - |

Noncash investing and financing activities -

2001 -

Exchange of common stock for a reduction in a note payable from a related party of \$100,000 and interest of \$20,000.

Exchange of common stock for Board of Directors fees of \$78,000

Exchange of redeemable common stock upon legal settlement of \$150,000.

Exchange of common stock for legal services of \$202,500.

2000 -

Exchange of note receivable from related party of \$165,617 and \$134,383 of accrued interest thereon for acquisition of treasury stock.

The accompany notes are an integral part of these financial statements

AVIATION GENERAL, INCORPORATED AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2002 AND 2001

NOTE A - ORGANIZATION AND OPERATIONS

Aviation General, Incorporated (AGI) was incorporated August 4, 1998 under the laws of the State of Delaware, and is the successor to the operations of Commander Aircraft Company (CAC). AGI is a holding company which, through its wholly owned subsidiaries, CAC and Strategic Jet Services, Inc. (SJS) (collectively referred to as the Company), manufactures, markets, and provides support services for single engine, high performance Commander aircraft and to a lesser extent provides sales and service of other pre-owned aircraft. The Company also provides consulting, sales, brokerage, and refurbishment services for jet aircraft through SJS.

The Board of Directors of AGI is authorized to issue preferred stock in one or more series. The Board of Directors is further authorized to fix the number of shares constituting such series and to fix the relative rights and preferences of the shares of the series.

NOTE B - SUMMARY OF ACCOUNTING POLICIES

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A summary of the significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements follows.

1. Principles of Consolidation

The Company consolidates the accounts of its subsidiaries, CAC and SJS. All intercompany balances and transactions are eliminated in consolidation.

2. Cash and Cash Equivalents

The Company considers all highly liquid debt instruments purchased with a maturity of three months or less and money market funds to be cash equivalents. The Company maintains its cash in bank deposit accounts, which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risks on cash and cash equivalents. As of December 31, 2001, the Company had approximately \$212,000 on deposit at one financial institution. The Company had a bank overdraft of \$(2,145) at December 31, 2002.

3. Investments

The Company had an investment consisting of 245,000 shares of Stratesec Inc. common stock which had historically been classified as an available-for-sale security and reported at fair value with unrealized gains and losses excluded from earnings and reported in other comprehensive income.

However, during 2002, certain information has come to the Company's attention concerning the ability of Stratesec's stock to recover its fair value. Among these are deteriorating financial condition, the lack of development of merger or acquisition opportunities and notification from the American Stock Exchange on July 18, 2002 that Stratesec does not meet minimum equity requirements and is subject to being de-listed. Based on the above facts an impairment loss of approximately \$396,000 has occurred and has been recorded as a charge to earnings. At December 31, 2001, unrealized losses, net of income tax effects, of \$(253,873) had been recorded in accumulated other comprehensive income.

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3. Investments - Continued

The components of other comprehensive income (loss) are as follows for the years ended December 31:

| | 2002 | 2001 |
|---|------------|-------------|
| | ----- | ----- |
| Unrealized holding gains (losses) arising | | |
| during the period | \$ - | \$(440,640) |
| Less reclassification adjustment for net realized losses included in net income | 253,873 | 14,508 |
| Income tax benefit (expense) | - | 58,568 |
| | ----- | ----- |
| Other comprehensive income (loss) | \$ 253,873 | \$(367,564) |
| | ===== | ===== |

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4. Revenue Recognition

Sales of aircraft are recognized upon execution and funding of the purchase agreement and transfer of title to the buyer which occurs after the Company receives the airworthiness certificate from the Federal Aviation Administration (FAA). Additionally, for aircraft financed by the Company it must also be determined that the buyer's initial and continuing investments in the aircraft are adequate to demonstrate a commitment to pay. Sales of pre-owned aircraft are recognized upon execution and funding of the purchase agreement. Service revenue is recognized when the services are performed and billable.

5. Inventories

Inventories consist primarily of finished goods and parts for manufacturing and servicing of aircraft. Inventory costs include all direct manufacturing costs and applied overhead. These inventories, other than pre-owned aircraft, are stated at the lower of cost or market, and cost is determined by the average-cost method. Pre-owned aircraft are valued on a specific-identification basis at the lower of cost or current estimated realizable wholesale price. Inventory components were as follows at December 31, 2002:

| | 2002 ----- |
|----------------------------|-----------------------|
| Raw materials | \$ 1,321,993 |
| Work in process | 510,506 |
| New and pre-owned aircraft | 1,359,782 |
| Other | 19,250 |
| | ----- |
| | \$ 3,211,531 ===== |

During 2002 and 2001, certain indirect costs of manufacturing, primarily excess capacity costs, were considered abnormal and treated as current period charges rather than as a portion of inventory costs. Such costs, totaling approximately \$662,000 and \$991,000 for 2002 and 2001, respectively, are included in cost of sales - aircraft.

During 2002 the Company recognized an impairment loss of \$1,758,620 associated with writing the inventory to the lower of cost or market.

6. Property and Equipment

Depreciation is computed using the straight-line method for financial reporting purposes and accelerated methods for tax purposes over estimated useful lives of five to seven years for vehicles and aircraft, three to five years for office equipment and furniture, seven to ten years for leasehold improvements, and ten to fifteen years for manufacturing equipment and tooling.

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Depreciation expense was \$130,684 and \$120,098 for 2002 and 2001, respectively.

7. Income Taxes -----

Deferred income taxes are provided on carryforwards and on temporary differences between the tax basis of an asset or liability and its reported amount in the financial statements that will result in taxable or deductible amounts in future years. Deferred income tax assets and liabilities are determined by applying the presently enacted tax rates and laws.

The Company provides for a valuation allowance on deferred tax assets if, based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

AGI files a consolidated income tax return with its wholly owned subsidiaries.

8. Refundable Deposits -----

Refundable deposits consist of payments made by customers prior to having repairs performed on their aircraft and deposits on aircraft being produced. These deposits are recognized as revenue in the period the services are completed or the aircraft sale is recognized.

9. Prepaid Advertising and Advertising Costs -----

The Company expenses the cost of advertising as incurred, except for prepaid advertising. Prepaid advertising largely consists of costs for future magazine advertisements. These costs are expensed when the advertisements are published. Advertising expense for the years ended December 31, 2002 and 2001 was approximately \$5,363 and \$198,000, respectively.

10. Earnings (Loss) Per Common Share -----

Basic earnings (loss) per common share are calculated based on the weighted average number of common shares outstanding during the year, including redeemable common shares. Diluted earnings (loss) per common share has been computed based on the assumption that all dilutive options and warrants are exercised using the treasury stock method.

11. Use of Estimates -----

The preparation of the consolidated financial statements requires the use of management's estimates and assumptions in determining the carrying values of certain assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts for certain revenues and expenses during the reporting period. Actual results could differ from those estimates.

12. New Accounting Pronouncements -----

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In 2001, the Financial Accounting Standards Board issued new pronouncements: SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets.

SFAS No. 144 is effective for the Company for the fiscal year beginning January 1, 2002 and addresses accounting and reporting for the impairment or disposal of long-lived assets. SFAS No. 144 supersedes SFAS No. 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of, and Accounting Principles Board Opinion No. 30, Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business. SFAS No. 144 retains the fundamental provisions of SFAS No. 121 and expands the reporting of discontinued operations to include all components of an entity with operations that can be distinguished from the rest of the entity and that will be eliminated from the ongoing operations of the entity in a disposal transaction.

Management believes adoption of these new statements will not have any significant effect on the Company's financial condition or results of operations.

13. Going Concern

During the years ended December 31, 2001 and 2002, the Company incurred net (losses) of (\$5,519,592) and (\$4,285,111), respectively. As of December 31, 2002, the Company had a negative working capital of (\$1,729,244) and a deficit net worth of (\$2,623,575). On December 27, 2002 the Company's wholly owned subsidiary, Commander Aircraft Company, filed petitions for relief under Chapter 11 of the federal bankruptcy code. These factors raise substantial doubt about the Company's ability to continue as a going concern.

The ability of the Company to continue as a going concern is dependent upon the Company's ability to successfully reorganize Commander Aircraft Company, to attain a satisfactory level of profitability, and to obtain suitable and adequate financing. There can be no assurance that these objectives can be achieved. The financial statements do not include any adjustments that might result from the outcome of this uncertainty nor do they take into effect any adjustments that might occur as a result of a successful plan to reorganize Commander Aircraft Company. See Note C for further details.

14. Product Warranties and Liability

The Company follows the policy of accruing \$5,000 in projected product warranty cost associated with each new aircraft sold. Any portion of this accrual that is not used within the five year warranty period is recognized as income at the end of the warranty period. Costs exceeding the \$5,000 accrual per plane are charged to current operations as they are incurred and an additional accrual is recorded to cover the remaining warranty period on that plane. Warranty costs for the years ended December 31, 2002 and 2001 were \$61,052 and \$41,500, respectively.

The Company does not carry any product liability insurance and recognizes product liability costs at such time as a claim arises and an estimate of the ultimate liability associated with the claim can be determined. Product liability costs for the years ended December 31, 2002 and 2001 were \$200,000 and \$150,000, respectively.

15. Impairment of Long-Lived Assets

The Company evaluates long-lived assets for potential impairment in

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compliance with SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. The Company records impairment losses on long-lived assets used in operations when events and circumstances indicate the assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their carrying amounts. The Company has not recognized any impairments of its long-term assets that might occur as a result of its inability to continue as a going concern.

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NOTE C - PETITION FOR RELIEF UNDER CHAPTER 11

On December 27, 2002 the Company's wholly owned subsidiary, Commander Aircraft Company (the "Debtor") filed petitions for relief under Chapter 11 of the federal bankruptcy laws in the United States Bankruptcy Court for the District of Delaware. Under Chapter 11, certain claims against the Debtor in existence prior to the filing of the petitions for relief under the federal bankruptcy laws are stayed while the Debtor continues business operations as Debtor-in-possession. These claims are reflected in the December 31, 2002 balance sheet as "liabilities subject to compromise." Claims secured against the Debtor's assets ("secured claims") also are stayed, although the holders of such claims have the right to move the court for relief from the stay. Secured claims are secured primarily by liens on the Debtor's property, plant and equipment.

The Debtor received approval from the Bankruptcy Court to pay or otherwise honor certain of its prepetition obligations, including employee wages and product warranties totaling \$75,000.

NOTE C - NOTE RECEIVABLE

From time to time, the Company finances the sale of new aircraft with notes receivable from customers which are collateralized by the aircraft. At December 31, 2001, the Company had one note receivable which matures February 1, 2005 and bears interest at prime plus 1.5%. This note was paid in full during the year ended December 31, 2002.

NOTE D - NOTES PAYABLE

Notes payable consist of the following at December 31, 2002:

| | 2002 ----- |
|---|---------------|
| Revolving credit facilities (a) | \$1,359,819 |
| Note payable to individual, 0% interest, payable at confirmation of bankruptcy plan confirmation. | 200,000 |
| Note payable to an individual, payable December 31, 2004. Convertible to common stock at \$.85 a share. Interest due semi annually at the end of June and December until maturity. Collateralized by Commander Aircraft Company's inventory and fixed assets. | 1,000,000 |
| Note payable to individual, payable in monthly installments of \$8,699, including interest at 8%, through September 30, 2002; | |

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| | |
|------------------|-------------|
| uncollateralized | 34,795 |
| | ----- |
| | \$2,594,614 |
| | ===== |

(a) The revolving credit facilities may be drawn down to manufacture new and purchase pre-owned aircraft. Interest is payable monthly at fixed rates of 8% to 8.5% with specific draws and accrued unpaid interest thereon generally due within six months. The facilities are collateralized by specific new and pre-owned aircraft. The revolving credit facilities are subject to certain covenants and the Company was not in compliance with covenants on one of the facilities at December 31, 2002. In the bankruptcy plan of reorganization, the credit facilities are secured debt and are not impaired.

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NOTE E - DISCLOSURES ABOUT FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of each class of financial instruments as of December 31, 2002 and 2001. Such information does not purport to represent the aggregate net fair value of the Company:

Cash and Cash Equivalents. The balance sheet carrying amounts of cash and cash equivalents approximate fair values of such assets.

Note Receivable. The carrying amount approximates fair value because of the fluctuating interest rate associated with the note receivable.

Notes Payable. The carrying value of notes payable approximates fair value because of variable interest rates and the short-term nature of the instruments.

All of the Company's financial instruments are for purposes other than trading.

| | 2002 | |
|---------------------------------------|--------------------|---------------|
| | Carrying amount | Fair value |
| | ----- | ----- |
| Cash and cash equivalents (overdraft) | \$ (2,145) | \$ (2,145) |
| Notes payable | \$ (2,594,614) | (2,594,614) |

NOTE F - STOCK OPTION PLAN

In December 1993, the Company approved a stock option plan for issuance of options to purchase up to 300,000 shares of common stock to employees at the discretion of the committee appointed by the Board of Directors. The number of shares authorized for issuance has subsequently been increased to 3,300,000 shares. The stock option plan also provides for automatic grants of options to purchase 20,000 shares of common stock to each director on an annual basis. At December 31, 2002, approximately 952,000 shares remain to be granted under the plan. The stock options generally vest ratably over a three-year period and the

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exercise price of all options equaled or exceeded market price of the stock at the date of grant.

The Company uses the intrinsic value method to account for its stock option plan in which compensation is recognized only when the fair value of each option exceeds its exercise price at the date of grant. Accordingly, no compensation cost has been recognized for the options issued. Had compensation cost been determined based on the fair value of the options at the grant dates, the Company's net earnings (loss) and earnings (loss) per share would have been decreased/increased to the pro forma amounts for the years ended as indicated below.

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| | 2002 | 2001 | 2000 |
|--|---------------|---------------|-----------|
| Net (loss): | | | |
| As reported | \$(4,284,744) | \$(5,519,592) | \$450,033 |
| Pro forma | (4,397,114) | (5,932,547) | 17,407 |
| (Loss) per share, basic and diluted | | | |
| As reported | \$ (.60) | \$ (.84) | \$.07 |
| Pro forma | \$ (.62) | \$ (.90) | \$.01 |

NOTE F - STOCK OPTION PLAN - CONTINUED

The fair value of each grant is estimated on the date of grant using the Black-Scholes options-pricing model with the following weighted-average assumptions used for grants in 2002 and 2001, respectively: No expected dividends; expected volatility of 75% and 75%, risk-free interest rate of 4% and 4.3%, and expected lives of three years.

The Black-Scholes options pricing model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

A summary of the status of the Company's stock option plan as of December 31, 2002 and 2001 and changes during the years ending on those dates is presented below.

| | 2002 | | 2001 | |
|----------------------------------|-----------|--|-----------|--|
| | Shares | Weighted average exercise price | Shares | Weighted average exercise price |
| Outstanding at beginning of year | 2,655,550 | \$1.49 | 2,394,667 | \$2.15 |

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| | | | | |
|--|-----------|--------|-----------|--------|
| Granted | 661,000 | \$.33 | 1,123,383 | \$0.48 |
| Exercised | - | \$ - | - | - |
| Expired | (422,167) | \$1.60 | (117,500) | \$2.57 |
| Forfeited | (561,300) | \$1.39 | (745,000) | \$1.85 |
| Outstanding at end of year | 2,333,083 | \$1.14 | 2,655,550 | \$1.49 |
| Options exercisable at year end | 1,672,083 | \$1.44 | 993,076 | \$2.17 |
| Weighted average fair value of options granted during the year | | \$.17 | | \$0.23 |

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The following table summarizes information about fixed-price stock options outstanding at December 31, 2002:

| Range of exercise prices | Options outstanding | | | Options exercisable | |
|--------------------------|--------------------------------|---|---------------------------------|--------------------------------|---------------------------------|
| | Number outstanding at 12/31/02 | Weighted average remaining contractual life | Weighted average exercise price | Number exercisable at 12/31/02 | Weighted average exercise price |
| \$0.33 to \$1.38 | 1,529,017 | 1.97 | \$0.46 | - | |
| \$1.39 to \$1.75 | 77,500 | .88 | \$1.56 | 77,500 | |
| \$1.76 to \$2.75 | 726,566 | .67 | \$2.53 | 726,566 | |
| | ----- | | | ----- | |
| \$0.50 to \$2.75 | 2,333,083 | | | 804,066 | |
| | ===== | | | ===== | |

NOTE G - LEASES

The Company leases office space, hangar space, its manufacturing and service facility, and certain office equipment under agreements classified as operating leases that expire at various dates through 2004. Rental expense under these leases was approximately \$287,000 and \$287,000 for the years ended December 31, 2002 and 2001, respectively.

The Company's lease for office space, hangar space, and its manufacturing and service facility was a revocable permit to lease the facility. The permit required monthly rentals in the same amounts as the original lease. The permit further required the Company to pay outstanding delinquent amounts plus penalties as defined in the permit. On April 23, 2003, the Company transferred its lease to a third party. The Company negotiated a 3.5 year sub-lease with this third party for 50,011 square feet of manufacturing, service and office space, guaranteed renewable at six month intervals. The Company also agreed to pay \$94,359 in past due rent to this third party.

The future annual minimum lease payments under the April 23, 2003 operating lease are as follows:

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| | | |
|--------------------------|-------------------------------------|-----------|
| Year ending December 31, | | |
| | 2003 | \$ 75,600 |
| | 2004 | 113,400 |
| | 2005 | 113,400 |
| | 2006 | 94,500 |
| | | ----- |
| | Total future minimum lease payments | \$396,900 |
| | | ===== |

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NOTE H - SALES CONCENTRATIONS

The geographic sales of the Company's new aircraft are as follows:

| | 2002 | | 2001 | |
|---------------|--------|-------------|--------|-------------|
| | Number | Amount | Number | Amount |
| United States | 6 | \$3,758,426 | 7 | \$3,883,801 |
| Europe | - | | 1 | 505,225 |

Pre-owned aircraft sold during 2002 in the United States was 16, totaling \$3,654,093. Brokerage commissions of \$138,482 were received in 2002 as a selling agent for pre-owned aircraft.

Pre-owned aircraft sold during 2001 in the United States was 15, totaling \$3,413,533. Brokerage commissions of \$225,104 were received in 2001 as a selling agent for pre-owned aircraft.

NOTE I - RELATED PARTY TRANSACTIONS

On May 9, 2001, the Company entered into a \$200,000 unsecured note payable bearing interest at 9% and due on demand with a Company controlled by the Chairman of the Board of Directors. On August 3, 2001, the Company issued 200,000 shares of common stock having a fair value at the date of issue of \$120,000 in exchange for a \$100,000 reduction in the note payable and interest expense of \$20,000. On October 18, 2001, the affiliate assigned the note payable with an outstanding balance of \$85,000 to a stockholder.

During 2001, 130,000 shares of common stock having a fair value at the date of issue of \$78,000 were issued to members of the Board of Directors in exchange for services provided. During 2002, 115,152 shares of common stock having a fair value at the date of issue of \$45,000 were issued to members of the Board of Directors in exchange for services provided.

At December 31, 2001, amounts payable for brochures and publications to a company controlled by the Chairman of the Board of Directors were approximately \$33,000. Purchases from this entity were approximately \$38,000 and \$15,000 for the years ended December 31, 2001 and 2000. There were no purchases from this entity in 2002.

In prior years, the Company extended financing for aircraft and spare parts

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sold either directly to a director of the corporate general partner of the Company's majority stockholder or to an Authorized Sales and Service Representative (ASSR) owned by the director under a line of credit of \$5,000,000. The Company has made efforts to collect amounts owed under this line, including repeated requests for payment, attempts to obtain or cancel approximately 800,000 shares of common stock of the Company collateralizing the line and attempts to block ownership transfers of said shares. However, during 2001, the ASSR went out of business and the individual suffered other business reversals. In addition, the individual resigned from the Company's Board of Directors in 2001 and all of his stock options were cancelled. Due to the uncertainties relating to ultimate collectibility, during the fourth quarter of 2001, the Company recorded bad debt expense relating to this line of credit for the outstanding balance of \$1,529,889. In addition, the Company wrote off accrued, unpaid interest of \$115,977. Bad debt expense of \$1,529,889 is recorded in other operating expenses and the write-off of interest of \$115,977 is recorded as an offset to interest income in the 2001 statement of operations. Management intends to continue to attempt to collect on amounts owed and continue to attempt to take possession of the common stock collateralizing the line.

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NOTE J - INCOME TAXES

No current or deferred tax provision (benefit) has been recognized in the accompanying statements of operations given the historical operating losses incurred.

Components of the net deferred tax assets (liabilities) rounded to the nearest thousand are as follows at December 31, 2002:

| | 2002 |
|--|--------------|
| | ----- |
| Deferred tax assets (liabilities) | |
| Note receivable from related party | \$ 613,000 |
| Inventories | 1,152,000 |
| Depreciation and amortization | (106,000) |
| Unrealized losses (gains) on investments | - |
| Accrued liabilities | 98,000 |
| Net operating loss carryforwards | 13,600,000 |
| | ----- |
| Valuation allowance | 15,357,000 |
| | (15,357,000) |
| | ----- |
| Total deferred tax liabilities | \$ - |
| | ===== |

The valuation allowance on tax assets increased \$1,655,000 and \$2,418,000 in 2002 and 2001, respectively, primarily due to the generation of net operating loss carryforwards in both years.

The Company's net operating loss carryforwards will expire as follows:

Year ending December 31,

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| | |
|--|---------------|
| 2005 | \$ 2,998,231 |
| 2006 | 17,434 |
| 2007 | 6,466,819 |
| 2008 | 3,982,473 |
| 2009 | 4,523,401 |
| 2010 | 2,279,486 |
| 2011 | 3,445,366 |
| 2012 | 1,869,674 |
| 2018 | 1,681,538 |
| 2019 | 438,829 |
| 2021 | 3,298,986 |
| 2022 | 2,888,549 |
| | ----- |
| Total net operating loss carryforwards | \$ 33,890,786 |
| | ===== |

NOTE K - COMMITMENTS AND CONTINGENCIES

The Company is subject to regulation by the FAA. The Company is subject to inspections by the FAA and may be subjected to fines and other penalties (including orders to cease production) for noncompliance with FAA regulations. The Company has a Production Certificate from the FAA which delegates to the Company the inspection of each aircraft. The sale of the Company's product internationally is subject to regulation by comparable agencies in foreign countries.

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The Company faces the inherent business risk of exposure to product liability claims. In 1988, the Company agreed to indemnify a former manufacturer of the Commander single engine aircraft against claims asserted against the manufacturer with respect to aircraft built from 1972 to 1979. In 1994, Congress enacted the General Aviation Revitalization Act, which established an 18-year statute of repose for general aviation aircraft manufacturers. This legislation prohibits product liability suits against manufacturers when the aircraft involved in an accident is more than 18 years old. This action effectively eliminated all potential liability for the Company with respect to aircraft produced in the 1970s. The Company's product liability insurance policy with coverage of \$10 million per occurrence and \$10 million annually in the aggregate with a deductible of \$200,000 per occurrence and annually in the aggregate expired March 1, 1995. Subsequent to March 1, 1995, the Company is not insured for product liability claims.

During 2001, the Company executed an employment contract with its President and Chief Executive Officer through August 2006 which provides for a specified annual salary, subject to periodic adjustments and incentives. Should the Company terminate this executive without cause (as defined), the Company will be obligated to pay the executive an amount equal to his salary in effect at termination through the expiration of the term of the agreement. Further, should a termination without cause occur within two years following a change in control (as defined), the Company will pay the executive an additional amount equal to 2.99 times the executives salary in effect at the time of such change in control. The contract also includes a noncompete clause effective throughout the term of the employment contract and for a period of one year thereafter.

During 2001, the Company executed a consulting agreement with a member of the Board of Directors. The agreement provides for a consulting fee of \$60,000

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over an initial one-year term. The agreement renews automatically for successive one-year periods unless terminated by either party upon 90 days prior written notice. Upon termination of the agreement without cause (as defined), the Company would be obligated through the remainder of the then-current term of the agreement. The agreement also includes a noncompete clause effective throughout the term of the agreement and for a period of six months thereafter.

The Company is routinely involved in various legal matters arising in the normal course of business. Management believes that losses, if any, arising from such actions will not have a material adverse effect on the financial position or operations of the Company.

On September 24, 2002 the Company's common stock was delisted from the Nasdaq SmallCap Market and began trading on the Over-the-Counter Bulletin Board, or OTCBB, under the symbol AVGE.OB due to the Company's noncompliance with the applicable minimum asset and equity requirements and the minimum bid price requirement .

NOTE L - REDEEMABLE COMMON STOCK

On October 3, 2001, the Company, pursuant to an agreement, issued 150,000 shares of common stock. Under the agreement, the Company will be obligated for the difference between the net proceeds to the holder and \$150,000 should the holder elect to sell the shares within 12 months of such shares becoming fully tradable or if such shares cannot be sold or are not fully tradeable within 13 months of issuance the Company is obligated to buy back the shares for \$150,000. As such, during 2001, the Company recorded redeemable common stock of \$150,000 for the estimated fair market value of the redeemable securities issued.

NOTE M - STOCKHOLDERS' EQUITY

In connection with the following Shareholder Rights Agreement, the Company created a series of 100,000 shares of preferred stock, par value \$.01 per share, designated as Series A Junior Participating Preferred Stock (Series A Preferred Stock).

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During 2001, the Company adopted a Shareholder Rights Agreement providing each outstanding share of common stock with a Series A preferred share purchase right (right) that expires in July of 2011. Each right entitles the holder to purchase one one-thousandth of a share of Series A preferred stock at a price of \$10 per one one-thousandth of a share of Series A preferred stock. The rights will generally become exercisable only if a person or group (acquiring group), excluding the Company's largest stockholder, acquires, without approval of the Company's Board of Directors, 15% or more of the Company's common stock or announces a tender offer with the intention to do the same. Upon exercise, each holder, excluding the acquiring group, will receive the number of shares of common stock having a value equal to two times the exercise price of the right or one one-thousandth of a share of Series A preferred stock. The number of shares issuable upon exercise of rights is subject to certain antidilution adjustments. Generally, the rights may be redeemed by the Company at \$.01 per right. The rights are non-participating and non-voting until exercised.

Series A preferred stock issued, if any, upon exercise of the rights will be entitled to the greater of a cumulative quarterly dividend payment of \$10 per share when, and if, declared or 1,000 times the dividend declared per common share. In the event of liquidation, the Series A preferred share holders will be entitled to the greater of \$1,000 per share or an aggregate payment of 1,000 times the aggregate payment per common share. Each share of Series A preferred stock will be entitled to 1,000 votes on all matters submitted to the

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stockholders. The Series A preferred stock will not be redeemable or convertible into common stock or any other security of the Company.

NOTE N - EMPLOYEE BENEFIT PLANS

The Company has a profit sharing 401(k) plan covering substantially all employees. Eligible employees may contribute up to 15% of their compensation. The Company contributes an amount equal to at least 25% of each employee's contributions not in excess of 10% of compensation. However, additional contributions may be made at the Company's discretion. Expense under the plan was approximately \$19,000 and \$20,000 for 2002 and 2001, respectively.

Through December 31, 2001, the Company had a contributory health care benefit plan covering substantially all employees and eligible dependents. The plan provided for covered major medical expense benefits subject to certain deductibles, coinsurance provisions, and lifetime maximums. Through October 31, 2001, the plan had certain stop-loss coverage under an insurance policy that provided for payments of covered benefits in excess of \$25,000 per year per covered person. The policy also provided an aggregate monthly stop-loss for the plan based on number of covered persons. Effective October 31, 2001, due to a lapse in insurance coverage, the Company became uninsured on this plan for benefit claims occurring through December 31, 2001. As of January 1, 2002, the Company terminated its employee health care benefits. Management has accrued amounts, which it believes are sufficient to cover claims for incidents occurring from October 31, 2001 through December 31, 2001. Expense under the plan was approximately \$26,117 and \$338,000 for 2002 and 2001, respectively.

NOTE O - SEGMENT INFORMATION

The Company operates in the segments of piston engine aircraft manufacturing sales and service and jet aircraft brokerage and refurbishment. Information concerning the Company's reportable segments are as follows for the years ended December 31:

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| | 2002 | 2001 |
|--|----------------|----------------|
| | ----- | ----- |
| Revenues: | | |
| Jet aircraft brokerage and refurbishment | \$ 122,732 | \$ 95,000 |
| Aircraft sales and service | 8,320,684 | 9,392,795 |
| | ----- | ----- |
| Total | \$ 8,443,416 | \$ 9,487,795 |
| | ===== | ===== |
| Operating income (loss): | | |
| Jet aircraft brokerage and refurbishment | \$ 19,732 | \$ (223,486) |
| Aircraft sales and service | (3,410,650) | (4,670,771) |
| | ----- | ----- |
| Total | \$ (3,390,918) | \$ (4,894,257) |
| | ===== | ===== |
| Assets: | | |
| Jet aircraft brokerage and refurbishment | \$ - | \$ 3,871 |
| Aircraft sales and service | 3,715,022 | 7,299,986 |

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| | | | |
|------------------------------------|---------------|----------------|--------------|
| | ----- | ----- | |
| Total | \$ 3,715,022 | \$ 7,303,857 | |
| | ===== | ===== | |
| | Jet aircraft | Aircraft sales | Consolidated |
| | brokerage and | and service | total |
| | refurbishment | | |
| | ----- | ----- | ----- |
| Other significant items - 2002: | | | |
| Interest income | \$ - | \$ 1,929 | \$ 1,929 |
| Interest expense | - | 243,414 | 243,414 |
| Depreciation and amortization | - | 130,684 | 130,684 |
| Expenditures for long-lived assets | - | - | - |
| Other significant items - 2001: | | | |
| Interest income | \$ 566 | \$ 14,784 | \$ 15,350 |
| Interest expense | - | 498,715 | 498,715 |
| Depreciation and amortization | 1,487 | 118,611 | 120,098 |
| Expenditures for long-lived assets | - | 37,243 | 37,243 |

NOTE P - EARNINGS (LOSS) PER SHARE

The following table sets forth the computation of earnings (loss) per share and earnings (loss) per share assuming dilution at December 31:

| | | |
|---|----------------|----------------|
| | 2002 | 2001 |
| | ----- | ----- |
| Numerator | | |
| Net (loss) | \$ (4,284,744) | \$ (5,519,592) |
| Denominator for earnings (loss) per share | | |
| Weighted average shares outstanding, basic | 7,143,250 | 6,581,467 |
| Effect of dilutive securities - stock options | - | - |
| Denominator for earnings (loss) per share assuming dilution | 7,143,250 | 6,581,467 |
| (Loss) per share, basic | \$ (.60) | \$ (.84) |
| (Loss) per share, assuming dilution | \$ (.60) | \$ (.84) |

Outstanding options of 2,655,550, and 1,278,366, for the years ended December 31, 2002, and 2001, respectively, have been excluded from the above calculations as they would be antidilutive.

NOTE Q - MANAGEMENT PLANS

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During the second half of 2002, the Company experienced an abrupt lull and slowdown of its business, evidenced by cancellation or postponement of several new and pre-owned aircraft orders and the absence of prospective new business. Management continued to reduce its overhead expenses including employee layoffs, terminating the business operations of Strategic Jet Services, Inc., and suspending new aircraft production.

On December 27, 2002, Commander Aircraft Company filed a voluntary petition under Chapter 11 of the United States Bankruptcy Code for the District of Delaware. Management's plan was to go forward and:

- Continue CAC's operations and provide service and support to the fleet of Commander aircraft owners, refurbishment services, parts, and pre-owned aircraft brokerage.
- Secure adequate Debtor in Possession ("DIP") financing to allow CAC to continue to operate.
- Develop, secure, and establish investor funding for a financial reorganization plan that would allow CAC to emerge from bankruptcy to the satisfaction of its creditors and with minimal dilution to its shareholders.

Management has been successful in fulfilling these objectives, culminating in a court-confirmed reorganization plan, dated December 10, 2003, with the effective date scheduled for on or before March 31, 2004, unless extended, with Tiger Aircraft LLC or affiliate, which has been providing CAC with interim DIP financing, as the investor.

Pursuant to the confirmed bankruptcy plan and agreement with Tiger, Tiger will invest approximately \$2.8 million in Aviation General, Incorporated in return for an 80% ownership interest in AGI. Approximately \$2 million will be used to settle with creditors in accordance with CAC's bankruptcy plan, and the remainder will be used for working capital. Pursuant to the agreement with Tiger, AGI must secure the approval of the agreement from its shareholders as well as their authorization to amend the Company's Certificate of Incorporation to increase the Company's authorized common shares from 20,000,000 shares to 100,000,000 shares. The Company currently has 20,000,000 common shares authorized and approximately 7,000,000 common shares (excluding Treasury stock which will be retired) issued and outstanding. The agreement with Tiger will necessitate the issuance of approximately 28,000,000 new common shares of stock to Tiger, resulting in a total of approximately 35,000,000 shares issued and outstanding.

CAC plans to resume new aircraft production following the consummation of the transaction with Tiger and proceed to operate within the business model and strategies articulated in this document.

NOTE R - SUBSEQUENT EVENTS

On December 10, 2003 the Company's wholly owned subsidiary, Commander Aircraft Company (Commander), received confirmation of the First Amended Plan under Chapter 11 of the Bankruptcy Code filed by Commander on July 5, 2003 as amended on July 30, 2003 and December 10, 2003. The plan outlines the classes of claims and their treatments as follows:

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Class A (Administrative Claims). Class A consists of Administrative Claims, including Professional Claims, whether secured or unsecured, including the Debtor in Possession Loan. Claims in Class A approved and Allowed by the Court

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shall be paid in full, in cash, by Commander on the Effective Date of the Plan or as soon thereafter as the amount thereof can be fixed, unless a different treatment is agreed to or provided for in this Plan. Administrative Claims which by their terms are not due and payable on or before the Effective Date shall be paid as and when due. This class is not impaired. As of December 31, 2002 the Company had \$350,000 in Class A claims payable.

Class B (Priority Claims). Class B consists of Priority Claims under 11 U.S.C. 507 other than Administrative Claims and Priority Tax Claims. Allowed Claims in Class B shall be paid in full, in cash, by Commander on the Effective Date of the Plan or as soon thereafter as the amount thereof can be fixed, unless a different treatment is agreed to or provided for in this Plan. This class is not impaired. As of December 31, 2002 the Company had \$112,000 in Class B claims payable.

Class C (Priority Tax Claims). Class C consists of Priority Tax Claims Pursuant to 11 U.S.C. 507(a)(8). In full and complete satisfaction of the obligation of Commander and all co-debtors (including responsible parties against whom trust fund taxes have been or may potentially be assessed) on Claims in Class C, such claims shall be paid in full in deferred cash payments, with simple interest at 6% p.a. running from the Effective Date of the Plan until paid, amortized over 20 equal quarterly payments. Any contrary interpretation of the foregoing provision notwithstanding, Commander shall pay each Class C claim or relevant portion thereof in full on or before the sixth anniversary of the assessment date of each portion of such claim; provided, however, that any Creditor to which this provision applies must apply all payments on Class C claims to such claims in the order of assessment. If a holder of a Class C claim declares Commander to be in default of Commander's obligations to it under the Plan, and such default is not cured within 20 days after receipt by Commander and its counsel of the notice thereof by certified mail, then the entire liability shall become immediately due and payable, and such creditor may exercise any rights available under applicable non-bankruptcy law to collect such liability from Commander or any co-debtor or responsible party. As of December 31, 2002 the Company had \$150,000 in Class C claims payable.

Class D (Secured Claim of Nyliak). Class D consists of the secured pre-petition claim of Nyliak Investments, LLC. The holder of the claim in Class D shall retain its pre-petition lien on the Commander's Assets, and Commander shall cure any pre- and post-petition arrearages (including all accrued interest at the non-default rate, fees, and other charges) in cash on the Effective Date of the Plan, and shall, on the Effective Date of the Plan, make a payment in the amount necessary to reduce the outstanding balance to \$500,000, which shall fully satisfy the replacement lien and administrative claim. Any non-monetary defaults of Commander and any co-Debtor existing on the Petition Date and/or the Effective Date shall be waived and deemed cured, with all interest paid at the non-default rate with no late fees. All pre-payment penalties shall be waived. Thereafter, Commander shall pay the claim in accordance with the contract terms, except that the following terms of the loan documents dated July 22, 2002 shall be deleted and of no further force or effect as to any party or guarantor to said documents: Securities Purchase Agreement, Section 4 ("Covenants," including reservation of shares), Section 5 ("Right of First Offer"), and Section 6 ("Transfer Agent Instructions"); Secured Convertible Note, Article I (option to convert note into AGI shares), Article III, Sections 3.2 and 3.2 (Redemption), Article IV, Section 4.2 (default for failure to issue conversion shares), and Article V, Section 5.10 (notice of corporate events); and the entirety of the Investor Rights Agreement. Tiger Aircraft, LLC, shall provide an additional guaranty to the Nyliak loan in a form substantially similar to that of the existing guarantors. Provided payments hereunder are not in default, the Debtor may sell Inventory in the ordinary course of business free and clear of the lien of Nyliak, which lien shall be replaced by a replacement lien on Inventory of the types to which its pre-petition lien attaches, manufactured or acquired

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after the Petition Date, in an amount equal to the value of the Nyltiak lien on Inventory sold after the Petition Date. This class is impaired. As of December 31, 2002, the Company had \$650,000 in Class D claims payable.

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Class E (Secured Claim of the IRS). Class E consists of the claim of the Internal Revenue Service secured by a pre-petition tax lien. In full and complete satisfaction of the obligation of Commander and all co-debtors (including responsible parties against whom trust fund taxes may potentially be assessed) on the claim in Class E, the holder of such claim shall retain its pre-petition lien until paid in full, and such claim shall be paid in full in deferred cash payments, with simple interest at 6% p.a. running from the Effective Date of the Plan until paid, amortized over 20 equal quarterly payments. If a holder of a Class E claim declares Commander to be in default of Commander's obligations to it under the Plan, and such default is not cured within 20 days after receipt by Commander and its counsel of the notice thereof by certified mail, then the entire liability shall become immediately due and payable, and such creditor may exercise any rights available under applicable non-bankruptcy law to collect such liability from Commander or any co-debtor or responsible party. Provided payments hereunder are not in default which has not been cured as provided in the preceding sentence, Commander may sell inventory in the ordinary course of business free and clear of the lien of the IRS, which lien shall be replaced by a replacement lien on inventory manufactured or acquired after the Petition Date in an amount equal to the value of the IRS lien on inventory sold after the Petition Date, said replacement lien to be junior to the lien of Nyltiak on inventory of the types to which Nyltiak's pre-petition lien attaches. This class is impaired. As of December 31, 2002, the Company had \$552,891 in Class E claims payable.

Class F (Secured Claim of Uptown Bank). Class F consists of the secured claim of Uptown National Bank of Chicago or its successor in interest, Bridgeview Bank and Trust. In full and complete satisfaction of the obligation of Commander and all co-debtors on the claim in Class F, the holder of the claim in Class F shall retain its pre-petition lien on Commander's assets, and Commander shall pay interest and other accrued charges through the Effective Date at the contract rate in cash on the effective date of the Plan. Thereafter, interest shall accrue at the rate of 8% p.a. on the outstanding principal balance allocable to each aircraft. Upon the sale of any aircraft which is Collateral for this claim, the Debtor shall pay the loan balance allocable to such aircraft in full, with all accrued interest and other charges, and the lien on such aircraft shall thereupon be released. Each 6 months after the Effective Date, the Debtor shall pay all accrued interest to date, plus a curtailment of 10% of the then-outstanding principal balance. In the event any portion of the claim remains unpaid on the second anniversary of the Effective Date, the Debtor shall, as to each aircraft which is Collateral for the Claim, either (a) fully pay in cash the balance of the claim allocable to such aircraft, or (b) surrender the aircraft to the Holder of the Claim in full satisfaction of the claim allocable to such aircraft. This class is impaired. As of December 31, 2002, the Company had \$1,242,648 in Class F claims payable.

Class G (Any other Secured Claim). Class G consists of any Allowed Secured Claim other than those in Classes A, D, E, F, J, or L. Any holder of an Allowed Claim in Class G shall retain its pre-petition lien on Commander's Assets, and Commander shall cure any pre- and post-petition arrearages in cash on the Effective Date of the Plan (such that the claim of the U.S. Department of Labor and any other such claim due in full under the terms thereof will be paid in cash on the Effective Date of the Plan). Any dispute as to the allowance of such Claim or the amount thereof, and/or the amount necessary to cure such arrearages shall be submitted to the Court for determination, with any undisputed amount paid on the Effective Date of the plan and any additional amount upon entry of a

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Final Order fixing the amount thereof. Any non-monetary defaults of Commander and any co-Debtor existing on the

Petition Date and/or the Effective Date shall be waived and deemed cured. Thereafter, Commander shall pay the claim in accordance with the contract terms or applicable law. With respect to the claim of the U.S. Department of Labor, to the extent of payments made under Classes B, I and/or J directly to the employees on whose behalf or for whose wages which the Department of Labor claim was brought, such payments shall be credited to the payment due on such claim to the Department of Labor. To the extent that the amounts reflected in the USDOL claim are not paid (either directly or to the wage claimants as provided herein) in full in cash by the Effective Date, the USDOL, seven days after written notice to the debtor, shall exercise any and all of its administrative and judicial remedies to collect any amounts due the

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USDOL from any debtor or non-debtor without further Court Order. This class is not impairedAs of December 31, 2002 the Company had \$78,841 in Class G claims payable.

Class H (Unliquidated tort/warranty claims for pre-petition personal injury, property damage, or wrongful or death). Class H consists of all tort and warranty claims for personal injury, property damage or wrongful death that were unliquidated or in litigation as of the Petition Date, including any subrogation claims. The claim(s) in Class H shall be paid a total of \$100,000.00 in cash on the Effective Date in full satisfaction of their claim(s) against Commander and Aviation General, Incorporated. In the event more than one such claim is filed before the Bar Date and is allowed, such amount shall be placed in an interest-bearing account until the allowed amount of the Class H claims is liquidated, such amount to be divided pro rata among the holders of such claims upon liquidation thereof. If there are no such claims ultimately allowed, or if such claims are allowed in an amount such that the Class H claims would receive less than a total of \$100,000 were they included in Class I, the Debtor shall apply the \$100,000 to the payment of the Class I Claims and the Class H Claims shall be treated as Class I claims. In the event that Class H votes to accept this Plan, no holder of a Class H claim objects to this Plan or appeals the Confirmation Order, and the holders of all Class H claims agree on or before the Effective Date on allocation of payments to the holders of Class H claims, the total payment to the holder(s) of Class H claims shall be increased to \$200,000.00 and shall be paid on the Effective Date in full satisfaction of such claims. This class is impaired. As of December 31, 2002, the Company had \$200,000 in Class H payables.

Class I (General Unsecured Claims). Class I consists of Unsecured Non-Priority Claims other than those in Class H, J, or L. General unsecured claims shall be paid as follows: \$500,000 shall be placed in an interest-bearing bank account on the Effective Date of the Plan, and shall be distributed pro rata to the holders of allowed Class I claims within 30 days of the Effective Date. The pro-rata share of the claimed amount of any claims which are then subject to objections as to which a Final Order has not been entered shall remain in the bank account until a Final Order is entered. When Final Orders are entered disallowing or allowing and liquidating all Class I claims, the remaining funds in the bank account shall be distributed to the holders of all Class I claims pro rata. This class is impaired. As of December 31, 2002, the Company had \$1,810,000 in Class I payables.

Class J (Small Claims administrative convenience class). Class J consists of any Claims (other than Class K or L claims) in an amount less than \$500.00, or as to which the holder thereof elects to receive treatment as a Class J claim. Class J claims shall be paid in cash on the Effective Date of the Plan in

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the allowed amount thereof (or \$500.00 in the event of holders of claims in other classes electing treatment under Class J), in full satisfaction of such claims. This class is not impaired. As of December 31, 2003, the Company had \$12,500 in Class J payables.

Class K (Equity Claims). Class K consists of any Claims based upon Equity Interests. The existing stock of the Debtor, 100% of which is owned by Aviation General, Incorporated, shall be cancelled. This class is impaired.

Class L (Corporate Family Claims). Class L consists of any Claims of Aviation General, Incorporated, and/or Strategic Jet Services, Inc. Class L claims shall be discharged and shall not be paid; in consideration thereof, all claims of Commander and the Estate against Aviation General, Incorporated ("AGI"), and/or Strategic Jet Services, Inc. ("SJS"), existing as of the Confirmation Date shall be released. Nothing in this plan shall relieve AGI or SJS of any obligation to the Debtor expressly set forth in this Plan, nor of any obligation owed directly to any Creditor.

Commander will fund this Plan primarily from the issuance of new stock. Commander's existing 100% shareholder, Aviation General, Incorporated ("AGI"), has agreed to purchase, on the Effective Date of the Plan, 2000 newly-issued shares of the stock of Commander, which stock shall be sold to it for \$1000 per share (\$2,000,000). Such shares shall not be subject to Nyliak's lien. To the extent additional funds are needed to implement this Plan or for working capital, AGI has agreed to purchase at that same price up to 800 additional shares of stock of Commander (\$800,000), upon the request of Commander, at any time during the 5 years after the Effective Date of the Plan.

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AGI shall fund this acquisition through the sale to Tiger Aircraft, LLC, of shares constituting 80% of the share capital of AGI for a total purchase price of \$2.8 million (of which \$2.3 million will be paid in cash on the effective date and \$500,000 in a demand note at 6% interest). Tiger shall also guarantee payment of the remaining claim in Class D, and shall guarantee AGI's performance of Commander's option to sell the 800 additional Commander shares at \$1000/share.

"Effective Date" means March 31, 2004, or such earlier date as Tiger, AGI, and Commander may jointly agree upon, provided that the Effective Date may not be earlier than the first Business Day after the Confirmation Order becomes a Final Order. The date of March 31, 2004, may be extended only on written consent of counsel for the Creditors Committee, counsel for the U.S. Department of Labor, and counsel for Nyliak Investments, LLC. In the event that Tiger does not close under the Stock Purchase Agreement by March 31, 2003 (or such later date as may be agreed by the Debtor, AGI, Tiger, the Committee, the DoL, and Nyliak), this Confirmation Order shall be void and of no further force or effect

The following is a summary of the quarterly results of operations for the years ended December 31:

| | 2002 | | | |
|---------------------|-------------|-------------|--------------|-------------|
| | March 31 | June 30 | September 30 | December 31 |
| Total net sales | \$1,504,821 | \$4,729,309 | \$ 1,674,338 | \$ 534,948 |
| Gross margin | 272,232 | 108,986 | 47,220 | 505,543 |
| Net loss | (290,185) | (411,956) | (1,288,804) | (2,294,166) |
| Net loss per share, | | | | |

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basic and diluted (0.04) (0.06) (0.18) (0.32)

| | 2001 | | | |
|--|--------------------|-------------|--------------|--------------|
| | Three months ended | | | |
| | March 31 | June 30 | September 30 | December 31 |
| Total net sales | \$2,639,760 | \$3,219,008 | \$ 1,552,396 | \$ 2,076,631 |
| Gross margin | 381,674 | 523,783 | 290,553 | (665,066) |
| Net loss | (598,587) | (455,408) | (559,764) | (3,905,833) |
| Net loss per share, basic and diluted | (0.10) | (0.07) | (0.08) | (0.59) |

| | 2000 | | | |
|--|--------------------|-------------|--------------|--------------|
| | Three months ended | | | |
| | March 31 | June 30 | September 30 | December 31 |
| Total net sales | \$3,942,575 | \$4,256,087 | \$ 4,804,798 | \$ 3,827,574 |
| Gross margin | 844,616 | 949,555 | 1,083,029 | 1,076,295 |
| Net income | 38,183 | 113,049 | 252,353 | 46,448 |
| Net income per share, basic and diluted | 0.01 | 0.02 | 0.04 | 0.01 |

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The sum of per-share amounts for the four quarters may differ from the annual per share amounts due to rounding and the required method of computing weighted average number of shares in the respective periods.

Item 9. Changes in and Disagreements with Accountants on Accounting and

Financial Disclosure.

On November 4, 2003, the Aviation General, Incorporated appointed Murrell, Hall, McIntosh & Co PLLP as its independent auditors.

On February 14, 2003, Grant Thornton LLP ("Grant Thornton") resigned as independent auditors of Aviation General, Incorporated (the "Registrant"). Grant Thornton advised the Registrant that the reason for its resignation was that it had determined that in light of the Registrant's financial condition and size, the Registrant does not meet Grant Thornton's current criteria for public-company audit clients.

The reports of Grant Thornton as of and for the fiscal years ended December 31, 2001 and 2000 did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope or accounting principles, except that the report on the Registrant's 2001 financial statements contained an explanatory paragraph describing an uncertainty about the Registrant's ability to continue as a going concern. During the two fiscal years ended December 31, 2001, and during the subsequent interim periods prior to February 14, 2003, there were no (i) disagreements between Grant Thornton and the Registrant on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedure, which disagreements, if

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not resolved to the satisfaction of Grant Thornton, would have caused it to make a reference to the subject matter of the disagreement in connection with its reports on the Registrant's financial statements, or (ii) events as described in Item 304(a)(1)(v) of Regulation S-K under the Securities Exchange Act of 1934, as amended, except as described below.

On February 21, 2003, the Registrant filed a report on Form 8-K disclosing the resignation of Grant Thornton, and on March 7, 2003 the Registrant filed an amendment to the report on Form 8-K. The March 7 amendment included as an exhibit a letter from Grant Thornton dated March 5, 2003. The Registrant is further amending the report on Form 8-K to include under this Item 4 the following language, which was contained in Grant Thornton's March 5 letter previously filed as an exhibit. References to "we" and "us" in this excerpt from Grant Thornton's letter refer to Grant Thornton.

"On January 10, 2003, the Registrant filed a Form 10-QSB/A for the period ended June 30, 2002, in which the Registrant reported that:

During the preparation of the third quarter 2002 financial statements, management identified certain excess capacity costs of approximately \$662,000 which were capitalized as work in process inventories as of June 30, 2002. Management believes these costs were incurred primarily as a result of the reduced manufacturing environment and should have been expensed during the second quarter 2002.

Management reported this improper capitalization to us in November 2002. By way of a letter dated February 14, 2003 (Internal Control Communication), we notified the Registrant's Management and Audit Committee of certain matters involving internal control and its operation that we considered to be reportable conditions under standards established by the American Institute of Certified Public Accountants. More particularly, we informed them that "the reportable condition relating to work in process inventory [that] included significant excess capacity costs that should have been expensed as incurred," in our view, constituted "a material weakness" We also noted in our Internal Control Communication that:

We have been informed that management took appropriate remedial actions to amend the second quarter interim financial statements and implemented additional controls to provide reasonable assurance that excess capacity costs are expensed and not capitalized as work in process inventory.

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Separately, and in addition to the matter involving the capitalization of excess capacity costs, we also pointed out in our February 14, 2003 Internal Control Communication that the Registrant's "current principal financial officer and existing accounting department staff may lack the requisite expertise needed for assessing and applying new and non-routine accounting principles and for preparing required financial and SEC reporting disclosures" and made recommendations for improvement."

We have responded to this concern by engaging the services of an outside Certified Public Accountant on a consulting basis to assist our principal financial officer with assessing and applying new and non-routine principles and in preparing financial and SEC reporting disclosures.

The Registrant furnished Grant Thornton with a copy of this amendment to its report and requested it to furnish the Registrant with a letter addressed to the Commission stating whether it agrees with the statements made by the Registrant in response to Item 304(a) of Regulation S-K and, if not, stating the respects

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in which it does not agree. A copy of Grant Thornton's letter is filed as Exhibit 16 to the amendment to Form 8-K.

In light of cost considerations and concerns that Grant Thornton has regarding their independence as a result of monies owned to them by the Company, the company has not received authorization from Grant Thornton to resubmit their audit of the Company's financial statements for the year ending December 31, 2001 which was included in the Company's 2001 which was included in the Company's 2001 10KSB previously filed and which is identical to that submitted herewith in the Company's 10KSB for 2002.

PART III

Certain information required by Part III is omitted from this report in that registrant will file a definitive proxy statement pursuant to Regulation 14A for its 2003 Proxy Statement, and the information included therein is incorporated by reference.

Item 10. Directors and Executive Officers of the Registrant

Information regarding directors of the Registrant required by this item is incorporated herein by reference to the Company's 2002 Proxy Statement under the caption "Election of Directors - Nominees".

The information regarding executive officers of the Company required by this item appearing in the Company's 2002 Proxy Statement under the caption "Election of Directors - Other Officers" is hereby incorporated by reference.

Item 11. Executive Compensation

The following table reflects the required disclosures regarding Executive Compensation for the years ended December 31, 2002 and 2001, respectively.

| | Year | Annual Compensation | | | Long-Term Compensation | | |
|--|------|---------------------|-------------|-------------|------------------------|---------------------------------------|--------------|
| | | Salary (1) | Bonus | Other | Awards | Securities Underlying Options Awarded | LTIP Payouts |
| | | (in shares) | (in shares) | (in shares) | (in shares) | | |
| Wirt D. Walker III | | | | | | | |
| Chairman and Chief Executive Officer | 2002 | \$ 127,846 | \$ - | - | 10,000 | 120,000 | - |
| | 2001 | \$ 128,077 | \$ - | - | - | 120,000 | - |
| Mat Goodman | | | | | | | |
| President/CEO Commander Aircraft Company, Inc. | 2002 | \$ 68,457 | \$ 3,950 | - | 48,485 | 50,000 | - |
| | 2001 | \$ 59,000 | \$70,072 | - | - | 53,133 | - |
| John DeHavilland | | | | | | | |
| Director | 2002 | \$ 56,646 | \$ - | - | - | - | - |

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| | | | | | | | |
|-------------------------|------|-----------|-----------|---|---|---------|---|
| | 2001 | \$ 89,231 | \$ 65,385 | - | - | 180,000 | - |
| Glenn A. Jackson | 2002 | \$ 9,646 | \$ - | - | - | - | - |
| Chief Financial Officer | 2001 | \$ - | \$ - | - | - | - | - |

- (1) Salary and bonus payments include voluntary salary reduction contributions to the Company's 401(k) savings plan
- (2) Amounts paid as director's fees unless otherwise indicated

Item 12. Security Ownership of Certain Beneficial Owners and Management

The following table sets forth as of December 31, 2002, certain information with respect to the beneficial ownership of the Company's Common Stock by (i) any person known by the Company to be the beneficial owner of more than 5% of the Company's voting securities, (ii) each director and each nominee for director to the Company, (iii) each of the executive officers named in the Summary Compensation Table appearing herein, and (iv) all executive officers and directors of the Company as a group.

| Name | Number of Shares | Percent of Total |
|---|------------------|------------------|
| Wirt D. Walker, III (1) (2) | 916,447 | 12.0% |
| N. Gene Criss (2) | 363,636 | 4.8% |
| John deHavilland (2) | 186,970 | 2.4% |
| Matthew J. Goodman (2) | 81,977 | 1.0% |
| Carl R. Gull (2) | 60,083 | * |
| Nyltiak Investments, LLC (3) | 1,176,471 | 15.1% |
| All Officers and Directors as a Group (5 persons) (4) | 1,609,113 | 21.1% |

* less than one percent

- (1) Includes 78,000 shares owned by a trust for the benefit of Mr. Walker's son and 117,000 shares owned by a trust for the benefit of Mr. Walker's mother, both of which Mr. Walker is the trustee. Does not include 261,714 shares owned by KuwAm Corporation, of which Mr. Walker is a Managing Director.
- (2) Includes shares issuable upon exercise of options that are exercisable within 60 days, as follows: Mr. Walker, 311,665 shares; Mr. Criss, 303,333 shares; Mr. DeHavilland, 126,667 shares; Mr. Goodman, 61,177 shares; and Mr. Gull, 60,083 shares.
- (3) Consists of shares that are issuable upon conversion of a convertible note held by Nyltiak Investments, LLC. James E. Lawson is the managing member of Nyltiak Investments and thus may be deemed to be the beneficial owner of shares owned by it.
- (4) On December 31, 2002, executive officers and directors of the Company as a group (5 persons) held options to purchase an aggregate of 1,661,083 shares of Common Stock, representing approximately 58.9% of outstanding options at that date. The numbers set forth in this table include an aggregate of

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862,925 shares underlying options, which are exercisable within 60 days of such date.

Item 13. Certain Relationships and Related Transactions

Note E - Disclosures About Fair Value of Financial Instruments and Note I - Related Party Transactions, of the Notes to Consolidated Financial Statements for 2002 are hereby incorporated by reference.

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PART IV

Item 14. Exhibits, Financial Statement Schedules, and Reports of Form 8-K:

| | Page |
|--|------|
| | ---- |
| (a) (1) The following financial statements are included in Part II Item 8: | |
| Report of Independent Public Accountants | 16 |
| Financial Statements: | |
| Consolidated Balance Sheets December 31, 2002 | 17 |
| Consolidated Statements of Operations for the years ended December 31, 2002 and 2001 | 19 |
| Consolidated Statement of Stockholders' Equity for the years ended 2002 and 2001 | 20 |
| Consolidated Statements of Cash Flows for the years ended December 31, 2002 and 2001 | 21 |
| Notes to Consolidated Financial Statements | 23 |
| (2) The following financial schedule for the years 2002 and 2001 is submitted herewith: | |
| Selected Quarterly Financial Data for the years ended December 31, 2002 and 2001 (unaudited) | |
| All other schedules are omitted because they are not applicable or the required information has been presented in the financial statements or notes thereto. | |
| (3) Exhibits included are hereby incorporated by reference to the Exhibit Index, page 48 of this report. | |

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INDEX OF EXHIBITS

| Exhibit No | Description |
|------------|---|
| 3.1 | Certificate of Incorporation of Aviation General, Incorporated. This exhibit is incorporated by reference to Exhibit 3.1 of the Registrant's Form S-4 filed June 12, 1998 (Reg. No. 333-56731). |
| 3.2 | Bylaws of Aviation General, Incorporated. This exhibit is incorporated by reference to Exhibit 3.2 of the Registrant's Form S-4 filed June 12, 1998 (Reg. No. 333-56731). |
| 4.1(a) | Certificate of Incorporation, describing the Common Stock (included in Exhibit 3.1). This exhibit is incorporated by reference to Exhibit 4.1(a) of the Registrant's Form S-4 filed June 12, 1998 (Reg. No. 333-56731). |
| 10.1 | Federal Aviation Administration ("FAA") Type Certificates issued to Commander Aircraft Company (the "Company") for models 112, 114, 112TC, 112B, 112TCA, 114A, and 114B. This exhibit is incorporated by reference to Exhibit 10.1 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128). |
| 10.2 | FAA Repair Station Air Agency Certificate issued to the Company. This exhibit is incorporated by reference to Exhibit 10.2 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128). |
| 10.3 | Lease and operations Agreement between the Company and the Trustees of the Oklahoma City Airport Trust dated August 9, 1988, as amended by the Supplemental Agreement No. 1 dated December 18, 1991, and the Supplemental Agreement No. 2 dated April 2, 1992. This exhibit is incorporated by reference to Exhibit 10.19 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128). |
| 10.4 | Textron Lycoming Finance Plan No. 1 between Textron Financial Corporation and the Company dated June 26, 1991, as amended to the Finance Plan No. 1 dated as of May 28, 1992, the Second Amendment dated as of September 29, 1992, and the Third Amendment dated as of December 10, 1992. This exhibit is incorporated by reference to Exhibit 10.29 of the Registrant's Form S-1 filed March 4, 1993 (Reg.No. 33-59128). |
| 10.5 | International Distributorship Agreement between the Company and Com-Air Flugzeughandel GmbH. This exhibit is incorporated by reference to Exhibit 10.31 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128). |
| 10.6 | International Distributorship Agreement between the Company and Aero Service b.v. This exhibit is incorporated by reference to Exhibit 10.32 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128). |
| 10.7 | International Dealership Agreement between the Company and Commander Khaleej Trading Establishment. This exhibit is incorporated by reference to Exhibit 10.28 of the Registrant's Form 10-K filed March 30, 1994. |
| 10.8 | Form of the Company's Authorized Sales and Service Representative Policy and Procedures Manual. This exhibit is incorporated by reference to Exhibit 10.37 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128). |

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10.9 Form of the Company's Authorized Sales and Service Representative Agreement. This exhibit is incorporated by reference to Exhibit 10.38 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128).

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10.10 Form of the Company's Service Center Agreement. This exhibit is incorporated by reference to Exhibit 10.39 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128).

10.11 The Commander Aircraft Company Profit Sharing Plan. This exhibit is incorporated by reference to Exhibit 10.40 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128).

10.12 Nonstatutory Stock Option Agreement between the Company and Wirt D. Walker III dated January 31, 1994. This exhibit is incorporated by reference to Exhibit 10.48 of the Registrant's Form 10-K filed March 30, 1994.

10.13 Nonstatutory Stock Option Agreement between the Company and Mishal Y.S. Al Sabah dated January 31, 1994. This exhibit is incorporated by reference to Exhibit 10.49 of the Registrant's Form 10-K filed March 30, 1994.

10.14 Form of Company's Aircraft Delivery and Acceptance Agreement. This exhibit is incorporated by reference to Exhibit 10.63 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128).

10.15 Form of the Company's Aircraft Retail Warranty. This exhibit is incorporated by reference to Exhibit 10.64 of the Registrant's Form S-1 filed March 4, 1993 (Reg. No. 33-59128).

10.16 Commander Aircraft Company 1993 Stock Option Plan. This exhibit is incorporated by reference to Exhibit 10.53 of the Registrant's Form 10-K filed March 28, 1996.

10.17 Security Purchase Agreement dated July 22, 2002 between Aviation General, Incorporated and Nytiak Investments, LLC filed August 14, 2002.

21 List of subsidiaries

31.2 Certification of Wirt D. Walker III

31.2 Certification of Glenn A. Jackson

32 Certification of Wirt D. Walker III and Glenn A. Jackson

Item 14. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. The Company's Chief Executive Officer and the Company's principal financial officer, after evaluating the effectiveness of the Company's disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rule 13a-14(c) and 15d-14(c) as of the date of the financial statements included in this report on Form 10KSB for December 31, 2002, have concluded that as of the evaluation date, the Company's disclosure controls and procedures were adequate and effective to ensure that material information relating to the Company and the Company's

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consolidated subsidiaries would be made known to them by others within those entities, particularly during the period in which this annual report on Form 10-KSB was being prepared.

Changes in Internal Controls. There were no significant changes in the Company's internal controls or in other factors that could significantly effect the Company's disclosure controls and procedures subsequent to the evaluation date, nor any significant deficiencies or material weaknesses in such disclosure controls and procedures requiring corrective actions. As a result, no corrective actions were taken.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto authorized on the 28th day of March 2001.

AVIATION GENERAL INCORPORATED

By:\s\ Wirt D. Walker III

Wirt D. Walker III

By:\s\ Glenn A. Jackson

Glenn A. Jackson

Pursuant to the requirements of the Securities and Exchange Act of 1934, this report has been signed above by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Principal Executive Officers:

| | | |
|--------------------|--|----------------|
| Wirt D. Walker III | Chairman Chief Executive Officer President | March 24, 2004 |
|--------------------|--|----------------|

Principal Financial Officer and Accounting Officer:

| | | |
|------------------|-------------------------|----------------|
| Glenn A. Jackson | Chief Financial Officer | March 24, 2004 |
|------------------|-------------------------|----------------|

Directors:

| | | |
|--------------------|----------|----------------|
| Wirt D. Walker III | Director | March 24, 2004 |
|--------------------|----------|----------------|

