

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE QUARTERLY PERIOD ENDED September 30, 2016

OR

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE TRANSITION PERIOD FROM _____ TO _____.

Commission file number 001-35927

Air Industries Group

(Exact name of Registrant as specified in its charter)

Nevada
(State or other jurisdiction of
incorporation or organization)

80-0948413
(IRS Employer
Identification No.)

360 Motor Parkway, Suite 100, Hauppauge, New York 11788
(Address of principal executive offices)

(631) 881-4920
(Issuer's telephone number)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer or a smaller reporting company. See definitions of "accelerated filer" "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer

Non-accelerated filer (do not check if smaller reporting company) Smaller reporting company

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

As of November 10, 2016, the registrant had outstanding 7,583,165 shares of common stock.

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, or Securities Act, and Section 21E of the Securities Exchange Act of 1934, or Exchange Act. Forward-looking statements are predictive in nature and can be identified by the fact that they do not relate strictly to historical or current facts and generally include words such as "expects," "anticipates," "intends," "plans," "believes," "estimates" and similar expressions. Certain of the matters discussed herein concerning, among other items, our operations, cash flows, financial position and economic performance including, in particular, future sales, product demand, competition and the effect of economic conditions, include forward-looking statements.

Although we believe that these statements are based upon reasonable assumptions, including projections of orders, sales, operating margins, earnings, cash flow, research and development costs, working capital, capital expenditures, distribution channels, profitability, new products, adequacy of funds from operations, and general economic conditions, these statements and other projections contained herein expressing opinions about future outcomes and non-historical information, are subject to uncertainties and, therefore, there is no assurance that the outcomes expressed in these statements will be achieved. Investors are cautioned that forward-looking statements are not guarantees of future performance and actual results or developments may differ materially from the expectations expressed in forward-looking statements contained herein. Given these uncertainties, you should not place any reliance on these forward-looking statements which speak only as of the date hereof. Factors that could cause actual results to differ materially from those reflected in the forward-looking statements include, but are not limited to, those discussed under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2015 and elsewhere in this report and the risks discussed in our other filings with the SEC.

We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future events or otherwise, except as may be required under the securities laws of the United States.

PART I

FINANCIAL INFORMATION

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AIR INDUSTRIES GROUP
Condensed Consolidated Balance Sheets

	<u>September 30,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
	<u>(Unaudited)</u>	
ASSETS		
Current Assets		
Cash and Cash Equivalents	\$ 1,297,000	\$ 529,000
Accounts Receivable, Net of Allowance for Doubtful Accounts of \$656,000 and \$985,000, respectively	9,935,000	13,662,000
Inventory	43,026,000	36,923,000
Prepaid Expenses and Other Current Assets	1,328,000	1,583,000
Assets Held for Sale Net	-	1,700,000
Total Current Assets	55,586,000	54,397,000
Property and Equipment, Net	16,238,000	15,299,000
Capitalized Engineering Costs - Net of Accumulated Amortization of \$4,875,000 and \$4,595,000, respectively	1,391,000	1,027,000
Deferred Financing Costs, Net, Deposits and Other Assets	1,136,000	1,094,000
Intangible Assets, Net	2,893,000	3,852,000
Deferred Tax Asset, Net	4,178,000	2,063,000
Goodwill	10,518,000	10,518,000
TOTAL ASSETS	\$ 91,940,000	\$ 88,250,000
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities		
Notes Payable and Capitalized Lease Obligations - Current Portion	\$ 34,106,000	\$ 40,893,000
Accounts Payable and Accrued Expenses	14,375,000	12,053,000
Deferred Gain on Sale - Current Portion	38,000	38,000
Deferred Revenue	1,070,000	958,000
Income Taxes Payable	34,000	14,000
Total Current Liabilities	49,623,000	53,956,000
Long Term Liabilities		
Notes Payable and Capitalized Lease Obligations - Net of Current Portion	8,493,000	3,912,000
Deferred Gain on Sale - Net of Current Portion	342,000	371,000
Deferred Rent	1,216,000	1,206,000
TOTAL LIABILITIES	59,674,000	59,445,000
Commitments and Contingencies		
Stockholders' Equity		
Preferred Stock, par value \$.001-Authorized 1,000,000 shares Designated as Series A Convertible Preferred Stock - par value \$.001, Authorized 900,000 shares, 732,297 shares and 0 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively, Aggregate liquidation preference \$7,322,970 and \$0 as of September 30, 2016 and December 31,2015, respectively.	1,000	-
Common Stock - par value \$.001 - Authorized 25,000,000 shares, 7,583,165 and 7,560,040 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	7,000	7,000
Additional Paid-In Capital	51,644,000	44,155,000
Accumulated Deficit	(19,386,000)	(15,357,000)
TOTAL STOCKHOLDERS' EQUITY	32,266,000	28,805,000
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 91,940,000	\$ 88,250,000

See Notes to Condensed Consolidated Financial Statements

AIR INDUSTRIES GROUP
Condensed Consolidated Statements of Operations
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Net Sales	\$ 15,710,000	\$ 21,076,000	\$ 50,257,000	\$ 56,944,000
Cost of Sales	13,713,000	16,898,000	41,284,000	44,500,000
Gross Profit	1,997,000	4,178,000	8,973,000	12,444,000
Operating Expenses	4,302,000	4,152,000	12,896,000	11,880,000
(Loss) Income from Operations	(2,305,000)	26,000	(3,923,000)	564,000
Interest and Financing Costs	(894,000)	(451,000)	(1,771,000)	(1,341,000)
Loss on extinguishment of debt	(172,000)	-	(172,000)	-
Other Income, Net	4,000	36,000	35,000	98,000
Loss before Income Taxes	(3,367,000)	(389,000)	(5,831,000)	(679,000)
Benefit from Income Taxes	1,320,000	726,000	2,102,000	519,000
Net (Loss) Income	(2,047,000)	337,000	(3,729,000)	(160,000)
Less: Cumulative preferred stock dividends	(252,000)	-	(334,000)	-
Net (Loss) Income attributable to common stockholders	\$ (2,299,000)	\$ 337,000	\$ (4,063,000)	\$ (160,000)
(Loss) Income per share - basic	\$ (0.30)	\$ 0.04	\$ (0.54)	\$ (0.02)
(Loss) Income per share - diluted	\$ (0.30)	\$ 0.04	\$ (0.54)	\$ (0.02)
Weighted average shares outstanding - basic	7,610,220	7,559,501	7,594,215	7,450,707
Weighted average shares outstanding - diluted	7,610,220	7,686,287	7,594,215	7,450,707

See Notes to Condensed Consolidated Financial Statements

AIR INDUSTRIES GROUP
Condensed Consolidated Statements of Cash Flows For the Nine Months Ended September 30,
(Unaudited)

	<u>2016</u>	<u>2015</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Loss	\$ (3,729,000)	\$ (160,000)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities		
Depreciation of property and equipment	2,808,000	2,679,000
Amortization of intangible assets	960,000	923,000
Amortization of capitalized engineering costs	280,000	238,000
Bad debt expense	(3,000)	76,000
Non-cash compensation expense	126,000	77,000
Amortization of deferred financing costs	356,000	142,000
Deferred gain on sale of real estate	(29,000)	(28,000)
Loss on sale of fixed assets held for sale	5,000	-
Deferred income taxes	(2,145,000)	(650,000)
Loss on extinguishment of debt	172,000	-
Amortization of convertible notes payable	184,000	-
Changes in Assets and Liabilities		
(Increase) Decrease in Operating Assets:		
Accounts receivable	3,730,000	(114,000)
Inventory	(6,389,000)	(10,031,000)
Prepaid expenses and other current assets	285,000	12,000
Deposits and other assets	(199,000)	(108,000)
Increase (Decrease) in Operating Liabilities:		
Accounts payable and accrued expenses	2,356,000	5,065,000
Deferred rent	10,000	26,000
Deferred revenue	112,000	475,000
Income taxes payable	(14,000)	(71,000)
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(1,124,000)	(1,449,000)
CASH FLOWS FROM INVESTING ACTIVITIES		
Capitalized engineering costs	(644,000)	(465,000)
Purchase of property and equipment	(1,341,000)	(967,000)
Proceeds from the sale of fixed assets	1,671,000	-
Cash paid for acquisitions	-	(6,945,000)
Cash acquired in acquisitions	-	605,000
NET CASH PROVIDED BY (USED IN) INVESTING ACTIVITIES	(314,000)	(7,772,000)
CASH FLOWS FROM FINANCING ACTIVITIES		
Note payable - revolver, net	(3,782,000)	10,328,000
Proceeds from note payable - term loans	-	3,500,000
Payments of note payable - term loans	(2,814,000)	(1,466,000)
Capital lease obligations	(908,000)	(487,000)
Proceeds from capital lease financing	-	500,000
Proceeds from issuance of preferred stock	5,250,000	-
Proceeds from notes payable issuances – related party	2,900,000	-
Proceeds from notes payable issuances	2,720,000	-
Deferred financing costs	(199,000)	(362,000)
Notes payable - sellers	-	(41,000)
Payments related to lease impairment	-	(44,000)
Expense for issuance of preferred stock	(663,000)	-
Expenses for issuance of convertible debt	(298,000)	-
Dividends paid	-	(3,334,000)
NET CASH PROVIDED BY FINANCING ACTIVITIES	2,206,000	8,594,000
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	768,000	(627,000)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	529,000	1,418,000
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 1,297,000	\$ 791,000

AIR INDUSTRIES GROUP
Condensed Consolidated Statements of Cash Flows For the Nine Months Ended September 30, (Continued)
(Unaudited)

	<u>2016</u>	<u>2015</u>
Supplemental cash flow information		
Cash paid during the period for interest	\$ 1,678,000	\$ 1,172,000
Cash paid during the period for income taxes	\$ 13,000	\$ 445,000
Supplemental disclosure of non-cash transactions		
Preferred stock issued for notes payable - related party	\$ 1,750,000	\$ -
Extinguishment of related party notes payable, net of issuance of convertible related party notes payable	\$ -	\$ -
Preferred shares issued for PIK dividends	\$ 300,000	-
Acquisition of property and equipment financed by capital lease	\$ 2,096,000	\$ 1,811,000
Dividends payable	\$ -	\$ 1,134,000
Placement agent warrants issued	\$ 26,000	\$ -
Purchase of assets of Compac and assumption of liabilities in the acquisition of liabilities in the acquisition as follows:		
Fair Value of tangible assets acquired	\$ -	\$ 406,000
Intangible assets	-	600,000
Goodwill	-	560,000
Liabilities assumed	-	(95,000)
Cash paid for acquisition	\$ -	\$ 1,471,000
Purchase of stock of The Sterling Engineering Corporation and assumption of liabilities in the acquisition as follows:		
Fair Value of tangible assets acquired	\$ -	\$ 8,281,000
Goodwill	-	3,346,000
Cash acquired	-	588,000
Liabilities assumed	-	(2,538,000)
Common stock issued	-	(4,203,000)
Cash paid for acquisition	\$ -	\$ 5,474,000

See Notes to Condensed Consolidated Financial Statements

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1. FORMATION AND BASIS OF PRESENTATION**Organization**

On August 30, 2013, Air Industries Group, Inc. ("Air Industries Delaware") changed its state of incorporation from Delaware to Nevada as a result of a merger with and into its newly formed wholly-owned subsidiary, Air Industries Group, a Nevada corporation ("Air Industries Nevada" or "AIRI") and the surviving entity, pursuant to an Agreement and Plan of Merger. The reincorporation was approved by the stockholders of Air Industries Delaware at its 2013 Annual Meeting of Stockholders. Air Industries Nevada is deemed to be the successor.

The accompanying consolidated financial statements presented are those of AIRI, and its wholly-owned subsidiaries; Air Industries Machining Corp. ("AIM"), Welding Metallurgy, Inc. ("WMI" or "Welding"), Miller Stuart, Inc. ("Miller Stuart"), Nassau Tool Works, Inc. ("NTW"), Woodbine Products, Inc. ("Woodbine" or "WPI"), Decimal Industries, Inc. ("Decimal"), Eur-Pac Corporation ("Eur-Pac" or "EPC"), Electronic Connection Corporation ("ECC"), AMK Welding, Inc. ("AMK"), Air Realty Group, LLC ("Air Realty"), The Sterling Engineering Corporation ("Sterling") effective March 1, 2015, and Compac Development Corporation ("Compac") effective September 1, 2015 (together, the "Company").

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with Rule 8-03 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, as filed with the Securities and Exchange Commission.

Reclassifications

Certain account balances in 2015 have been reclassified to conform to the current period presentation.

Note 2. ACQUISITIONS

The Company accounts for all business combinations in accordance with Financial Accounting Standards Board ("FASB") ASC 805, "Business Combinations" ("ASC 805"), using the acquisition method of accounting. Under this method, assets and liabilities, including any remaining non-controlling interests, are recognized at fair value at the date of acquisition. The excess of the purchase price over the fair value of assets acquired, net of liabilities assumed, and non-controlling interests is recognized as goodwill. Certain adjustments to the assessed fair values of the assets, liabilities, or non-controlling interests made subsequent to the acquisition date, but within the measurement period, which is up to one year, are recorded as adjustments to goodwill. Any adjustments subsequent to the measurement period are recorded in income. Results of operations of the acquired entity are included in the Company's results from the date of the acquisition onward and include amortization expense arising from acquired tangible and intangible assets. The Company expenses all costs as incurred related to an acquisition in the condensed consolidated statements of income.

Sterling

On March 1, 2015, the Company acquired all of the common stock of Sterling for \$5.4 million in cash and 425,005 shares of the common stock of AIRI. The common stock was valued at \$9.89 per share, which was the closing share price on February 27, 2015. The cash consideration is subject to adjustment for working capital changes. The Company has also entered into employment and non-compete agreements for two and three year periods with three of the principals of Sterling. The Company financed the acquisition of Sterling with the proceeds from the issuance of Term Loan D (see Note 7).

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Sterling founded in 1941 manufactures components for aircraft and ground turbine engines.

The acquisition of Sterling was accounted for under ASC 805. The purchase price allocation is set forth below.

Fair value of tangible assets acquired	\$	8,281,000
Goodwill		1,963,000
Cash acquired		588,000
Liabilities assumed		(1,216,000)
Total	\$	9,616,000

The below table sets forth selected unaudited proforma financial information for the Company as if Sterling were owned for the entire three and nine months ended September 30, 2015.

	Three Months Ended September 30, 2015	
Net Sales	\$	21,076,000
Income from operations	\$	26,000
	Nine Months Ended September 30, 2015	
Net Sales	\$	58,783,000
Income from operations	\$	711,000

The below table sets forth selected financial information for Sterling for the three and nine months ended September 30, 2016 and the portions of the three and nine months ended September 30, 2015 during which Sterling was a subsidiary of the Company.

	Three Months Ended	
	September 30, 2016	September 30, 2015
Net Sales	\$ 1,442,000	\$ 1,853,000
Loss from Operations	\$ (684,000)	\$ (570,000)
	Nine Months Ended	
	September 30, 2016	September 30, 2015
Net Sales	\$ 4,722,000	\$ 5,152,000
Loss from Operations	\$ (1,516,000)	\$ (585,000)

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principal Business Activity

AIM is primarily engaged in manufacturing aircraft structural parts, and assemblies for prime defense contractors in the aerospace industry in the United States. NTW is a manufacturer of aerospace components, principally landing gear for F-16 and F-18 fighter aircraft. Welding is a specialty welding and products provider whose significant customers include the world's largest aircraft manufacturers, subcontractors, and original equipment manufacturers. Eur-Pac's primary business is "kitting" of supplies for all branches of the United States Defense Department including ordnance parts, hose assemblies, hydraulic, mechanical and electrical assemblies. AMK is a provider of sophisticated welding and machining services for diversified aerospace and industrial customers. Sterling manufactures components for aircraft and ground turbine engines. Compac specializes in the manufacture of RFI/EMI (Radio Frequency Interference – Electro-Magnetic Interference) shielded enclosures for electronic components. The Company's customers consist mainly of publicly traded companies in the aerospace industry.

Inventory Valuation

The Company does not take physical inventories at interim quarterly reporting periods. Approximately 48% of the inventory value at September 30, 2016 has been estimated using a gross profit percentage based on sales of previous periods to the net sales of the current period, as management believes that the gross profit percentage on these items are materially consistent from period to period.

The remainder of the inventory value at September 30, 2016 is estimated based on the Company's standard cost perpetual inventory system, as management believes the perpetual system computed value for these items provides a better estimate of value for that inventory.

The Company valued inventory at December 31, 2015 at the lower of cost on a first-in-first-out basis or market.

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Credit and Concentration Risks

There was one customer that represented 14.2% and there were four customers that represented 55.3% of total sales for the three months ended September 30, 2016 and 2015, respectively. This is set forth in the table below.

Customer	Percentage of Sales	
	2016 (Unaudited)	2015 (Unaudited)
1	14.2	18.8
2	*	15.3
3	*	11.1
4	*	10.1

* Customer was less than 10% of sales for the quarter ended September 30, 2016

There were four customers that represented 53.3% and four customers that represented 62.1% of total sales for the nine months ended September 30, 2016 and 2015, respectively. This is set forth in the table below.

Customer	Percentage of Sales	
	2016 (Unaudited)	2015 (Unaudited)
1	19.8	17.0
2	11.9	14.9
3	10.9	17.3
4	10.7	12.9

There were three customers that represented 44.5% of gross accounts receivable and four customers that represented 61.1% of gross accounts receivable at September 30, 2016 and December 31, 2015, respectively. This is set forth in the table below.

Customer	Percentage of Receivables	
	September	December
	2016 (Unaudited)	2015
1	18.5	26.6
2	14.5	10.4
3	11.5	13.6
4	*	10.5

* Customer was less than 10% of Gross Accounts Receivable at September 30, 2016

As of September 30, 2016 and December 31, 2015, the Company had occasionally maintained balances in its bank accounts that were in excess of the FDIC limit. The Company has not experienced any losses on these accounts.

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

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Earnings per share

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

The following is a reconciliation of the denominators of basic and diluted earnings per share computations:

	Three Months Ended		Nine Months Ended	
	September 30, 2016	September 30, 2015	September 30, 2016	September 30, 2015
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Weighted average shares outstanding used to compute basic earnings per share	7,610,220	7,559,501	7,594,215	7,450,707
Effect of dilutive stock options and warrants	-	126,786	-	-
Weighted average shares outstanding and dilutive securities used to compute dilutive earnings per share	<u>7,610,220</u>	<u>7,686,287</u>	<u>7,594,215</u>	<u>7,450,707</u>

The following table sets forth the number of shares issuable upon exercise of outstanding options and warrants which were excluded from the diluted per share calculation because the exercise price was greater than the average market price of the common shares:

	Three and Nine Months Ended	
	September 30, 2016	September 30, 2015
	(Unaudited)	(Unaudited)
Stock Options	202,694	258,391
Warrants	-	46,800
	<u>202,694</u>	<u>305,191</u>

The following table sets forth the number of shares issuable upon conversion or exercise of outstanding convertible preferred stock, options and warrants which were excluded from the diluted per share calculation even though the exercise price was less than the average market price of the common shares and unvested restricted stock because the effect of including these potential shares was anti-dilutive due to the net loss applicable to common stockholders incurred during that period:

	September 30, 2016	September 30, 2015
	(Unaudited)	(Unaudited)
Convertible Preferred Stock	1,488,394	-
Stock Options	443,648	322,675
Warrants	519,573	117,785
Unvested Restricted Stock	52,000	-
	<u>2,503,615</u>	<u>440,460</u>

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with FASB ASC 718, "Compensation – Stock Compensation." Under the fair value recognition provision of the ASC, stock-based compensation cost is estimated at the grant date based on the fair value of the award. The Company estimates the fair value of stock options and warrants granted using the Black-Scholes-Merton option pricing model. Stock based compensation amounted to \$43,000 and \$23,000 for the three months ended September 30, 2016 and 2015, respectively, and \$126,000 and \$77,000 for the nine months ended September 30, 2016 and 2015, respectively, and was included in operating expenses on the accompanying Condensed Consolidated Statements of Operations.

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Goodwill

Goodwill represents the excess of the acquisition cost of businesses over the fair value of the identifiable net assets acquired. The goodwill amount of \$10,518,000 at September 30, 2016 and December 31, 2015 relates to the acquisitions of Welding \$291,000, NTW \$162,000, Woodbine \$2,565,000, Eur-Pac \$1,656,000, ECC \$109,000, AMK \$635,000, Sterling \$4,540,000 and Compac \$560,000. Goodwill is not amortized, but is tested for impairment annually, or if circumstances occur that more likely than not reduce the fair value of the reporting unit below its carrying amount.

The Company has determined that there has been no impairment of goodwill at September 30, 2016 and December 31, 2015.

Debt Issuance Costs

Effective January 1, 2016, the Company adopted FASB ASU 2015-15 “Interest-Imputation of Interest (Subtopic 835-30), Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements, Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting”. The amendments to the SEC paragraphs in this update state that given the absence of authoritative guidance within ASU 2015-03 for debt issuance costs related to line-of-credit arrangements, the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The adoption of this amended guidance did not have a significant impact on the Company’s consolidated financial statements.

Recently Issued Accounting Pronouncements

In January 2016, the FASB issued ASU 2016-01, “Recognition and Measurement of Financial Assets and Financial Liabilities (Subtopic 825-10)” (“ASU 2016-01”). The main objective of ASU 2016-01 is enhancing the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The amendments address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. ASU 2016-01 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company does not expect the adoption of this amendment to have a significant impact on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842)” (“ASU 2016-02”). The main objective of ASU 2016-02 is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. To meet that objective, the FASB is amending the FASB Accounting Standards Codification and creating Topic 842, Leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company does not expect the adoption of this amendment to have a significant impact on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, “Compensation—Stock Compensation (Topic 718) Improvements to Employee Share-Based Payment” (“ASU 2016-09”). ASU 2016-09 is part of the FASB Simplification Initiative. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of generally accepted accounting principles for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements. ASU 2016-09 will affect all entities that issue share-based payment awards to their employees. The areas for simplification involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company does not expect the adoption of these amendments to have a significant impact on its consolidated financial statements.

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In April 2016, the FASB issued ASU 2016-10 “Revenue from Contracts with Customers (Topic 606)” (“ASU 2016-10”). The core principle of the guidance in Topic 606 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments in ASU 2016-10 affect the guidance in ASU 2014-09, “Revenue from Contracts with Customers”, which is not yet effective. The effective date and transition requirements of ASU 2016-10 are the same as the effective date and transition requirements of ASU 2014-09. They are effective prospectively for reporting periods beginning after December 15, 2017 and early adoption is not permitted. The Company is currently assessing the impact of the adoption of these amendments on its consolidated financial statements.

In May 2016, the FASB issued Accounting Standards Update No. 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients. The amendments do not change the core revenue recognition principle in Topic 606. The amendments provide clarifying guidance in certain narrow areas and add some practical expedients. These amendments are effective at the same date that Topic 606 is effective. Topic 606 is effective for public entities for annual reporting periods beginning after December 15, 2017, including interim reporting periods therein (i.e., January 1, 2018, for a calendar year entity). Topic 606 is effective for nonpublic entities one year later. The Company is currently assessing the impact of the adoption of the amendments to Topic 606 and these amendments on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments”. The standard provides guidance on how certain cash receipts and payments are presented and classified in the statement of cash flows, including beneficial interests in securitization, which would impact the presentation of the deferred purchase price from sales of receivables. The standard is intended to reduce current diversity in practice. Early adoption is permitted, including adoption in an interim period. The Company does not expect the adoption of these amendments to have a significant impact on its consolidated financial statements.

Effective July 1, 2016, the Company adopted FASB Accounting Standards Update 2015-17, Balance Sheet Classification of Deferred Taxes. The ASU is part of the Board’s simplification initiative aimed at reducing complexity in accounting standards. To simplify presentation, the new guidance requires that all deferred tax assets and liabilities, along with any related valuation allowance, be classified as noncurrent on the balance sheet. As a result, each jurisdiction will now only have one net noncurrent deferred tax asset or liability. Importantly, the guidance does not change the existing requirement that only permits offsetting within a jurisdiction - that is, companies are still prohibited from offsetting deferred tax liabilities from one jurisdiction against deferred tax assets of another jurisdiction. The Company early adopted the new standard effective and reclassified the prior year deferred tax asset presented as of December 31, 2015 to conform with the new guidance.

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

Subsequent Events

Management has evaluated subsequent events through the date of this filing.

Note 4. PROPERTY AND EQUIPMENT

The components of property and equipment consisted of the following:

	September 30, 2016	December 31, 2015	
	(Unaudited)		
Land	\$ 300,000	\$ 300,000	
Buildings & Improvements	1,650,000	1,658,000	31.5 years
Machinery and Equipment	16,078,000	15,109,000	5 - 8 years
Capital Lease Machinery and Equipment	6,265,000	5,869,000	3 - 5 years
Capital Lease Facility	1,700,000	-	Term of Lease
Tools and Instruments	7,491,000	6,993,000	1.5 - 7 years
Automotive Equipment	217,000	191,000	5 years
Furniture and Fixtures	462,000	425,000	5 - 8 years
Leasehold Improvements	979,000	910,000	Term of Lease
Computers and Software	567,000	482,000	4-6 years
Total Property and Equipment	<u>35,709,000</u>	<u>31,937,000</u>	
Less: Accumulated Depreciation	<u>(19,471,000)</u>	<u>(16,638,000)</u>	
Property and Equipment, net	<u>\$ 16,238,000</u>	<u>\$ 15,299,000</u>	

Depreciation expense for the three months ended September 30, 2016 and 2015 was approximately \$957,000 and \$1,045,000, respectively. Depreciation expense for the nine months ended September 30, 2016 and 2015 was

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\$2,808,000 and \$2,679,000, respectively. Assets held under capitalized lease obligations are depreciated over the shorter of their related lease terms or their estimated productive lives. Depreciation of assets under capital leases is included in depreciation expense for 2016 and 2015. Accumulated depreciation on these assets was approximately \$2,056,000 and \$1,065,000 as of September 30, 2016 and December 31, 2015, respectively.

Note 5. INTANGIBLE ASSETS

The components of intangibles assets consisted of the following:

	September 30, 2016	December 31, 2015	
	(Unaudited)		
Customer Relationships	\$ 6,555,000	\$ 6,555,000	5 to 14 years
Trade Names	1,480,000	1,480,000	15 to 20 years
Technical Know-how	660,000	660,000	10 years
Non-Compete	150,000	150,000	5 years
Professional Certifications	15,000	15,000	.25 to 2 years
Total Intangible Assets	<u>8,860,000</u>	<u>8,860,000</u>	
Less: Accumulated Amortization	<u>(5,967,000)</u>	<u>(5,008,000)</u>	
Intangible Assets, net	<u>\$ 2,893,000</u>	<u>\$ 3,852,000</u>	

Amortization expense for the three months ended September 30, 2016 and 2015 was approximately \$320,000 and \$309,000, respectively. Amortization expense for the nine months ended September 30, 2016 and 2015 was approximately \$960,000 and \$923,000, respectively.

Note 6. SALE AND LEASEBACK TRANSACTION

On April 11, 2016, the Company executed a Sale - Leaseback Arrangement, whereby the Company sold the building and real property located in South Windsor, Connecticut (the "Property") for a purchase price of \$1,700,000. The net proceeds from the sale of the property were applied to the amounts owed to PNC Bank.

At September 30, 2016, the Company classified the Property as a Capital Lease Facility. The valuation of the property at the time of reclassification was \$1,700,000. Amortization expense for the three and nine months ended September 30, 2016 was approximately, \$9,000 and \$12,000, respectively.

Simultaneous with the closing of the sale of the Property, the Company entered into a 15-year lease (the "Lease") with the purchaser for the property. Base annual rent is approximately \$155,000 for the first year and increases approximately 3% per year, each year thereafter. The Lease grants the Company an option to renew the Lease for an additional period of five years. Pursuant to the terms of the Lease, the Company is required to pay all of the costs associated with the operation of the facilities, including, without limitation, insurance, taxes and maintenance. The Lease also contains representations, warranties, obligations, conditions and indemnification provisions in favor of the purchaser and grants the purchaser remedies upon a breach of the Lease by the Company, including the right to terminate the Lease and hold the Company liable for any deficiency in future rent.

The Company will account for the transaction under the provisions of FASB ASC 840-40, "Leases - Sale-Leaseback Transactions".

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Note 7. NOTES PAYABLE AND CAPITAL LEASE OBLIGATIONS

Notes payable and capital lease obligations consist of the following:

	September 30, 2016	December 31, 2015
	(Unaudited)	
Revolving credit note payable to PNC Bank N.A. ("PNC")	\$ 25,822,000	\$ 29,604,000
Term loans, PNC	7,019,000	9,833,000
Capital lease obligations	6,206,000	5,018,000
Related party notes payable	1,378,000	350,000
Notes payable (private placement)	2,174,000	-
Subtotal	42,599,000	44,805,000
Less: Current portion of notes and capital obligations	(34,106,000)	(40,893,000)
Notes payable and capital lease obligations, net of current portion	8,493,000	3,912,000

PNC Bank N.A. ("PNC")

The Company has a credit facility with PNC (the "Loan Facility") secured by substantially all of its assets. The Loan Facility has been amended many times during its term. The Loan Facility was amended in June 2016 (the "Twelfth Amendment") and September 2016 (the "Thirteenth Amendment"). In connection with the Twelfth Amendment, the Company paid PNC a fee of \$100,000 and reimbursed it for the fees and expenses of its counsel. The Twelfth Amendment provides for a \$33,000,000 revolving loan. In addition, in the Twelfth Amendment the four term loans (Term Loan A, Term Loan B, Term Loan C and Term Loan D) then outstanding were consolidated into a single term loan with the initial principal amount of \$7,387,854. Further, in the Twelfth Amendment the Company acknowledged that there were then outstanding excess advances under the revolving loan in the amount of \$12,500,000.

Under the terms of the Loan Facility, as amended, the revolving loan now bears interest at (a) the sum of the Alternate Base Rate plus one and three-quarters of one percent (1.75%) with respect to Domestic Rate Loans; and (b) the sum of the LIBOR Rate plus four and one-half of one percent (4.50%) with respect to LIBOR Rate Loans. The amount outstanding under the revolving loan, exclusive of the excess advance, was \$25,822,000 and \$29,604,000, as of September 30, 2016 and December 31, 2015, respectively.

The Loan Facility was further amended pursuant to the Thirteenth Amendment, to modify the advance rate with respect to our inventory to be the lesser of (i) 75% of the eligible inventory, an increase from 50%, and (ii) 90% of the liquidation value of the eligible inventory, an increase from 85%, subject to the inventory sublimit of \$12,500,000 and such reserves as PNC may deem proper. In addition, in the Thirteenth Amendment the lender waived any default resulting from the Company's obligation to comply with the minimum EBITDA covenant for the period ended June 30, 2016, consented to the issuance of the Company's 12% Subordinated Convertible Notes and the amendment to the Company's Articles of Incorporation to increase the authorized number of shares of Preferred Stock and Series A Preferred Stock.

The repayment terms of Term Loan A had been amended in April 2014, when the Company borrowed \$2,676,000, representing an additional \$1,328,000 to partially fund the acquisition of Woodbine. Term Loan A, as amended in 2014, was to be repaid in monthly installments of \$31,859 continuing until November 2016. On October 1, 2014, the Company borrowed \$3,500,000 under Term Loan B for the acquisition of AMK. Term Loan B was to be repaid in sixty consecutive monthly principal installments of \$58,333 continuing until November 2019.

Prior to the Twelfth Amendment, Term Loans A and B bore interest at (a) the sum of the Alternate Base Rate plus one and three quarters of one percent (1.75%) with respect to Domestic Rate Loans and (b) the sum of the LIBOR Rate plus three percent (3.00%) with respect to LIBOR Rate Loans.

On December 31, 2014, the Company borrowed \$2,500,000 under Term Loan C to refinance the Seller Note and Mortgage of \$2,500,000 issued as part of the acquisition of AMK. The maturity date of Term Loan C was the first business day of January 2021, and it was to be paid in seventy two consecutive monthly principal installments, which commenced on the first business day of February 2015, and continued on the first business day of each month

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thereafter. The first seventy-one of the installments were to be in the amount of \$34,722 with a seventy second and final payment of any unpaid principal and interest on the first business day of January 2021. Term Loan C bore interest at (a) the sum of the Alternate Base Rate plus two percent (2.00%) with respect to Domestic Rate Loans and (b) the sum of the LIBOR Rate plus three and one-quarter percent (3.25%) with respect to LIBOR Rate Loans.

On March 9, 2015, the Company borrowed \$3,500,000 under Term Loan D for the acquisition of Sterling. The repayment of Term Loan D consisted of twenty consecutive monthly principal installments, the first nineteen in the amount of \$62,847 which commenced on the first business day of April 2015, and continued on the first business day of each month thereafter, with a twentieth and final payment of any unpaid balance of principal and interest on the last business day of November 2016. Term Loan D bore interest at (a) the sum of the Alternate Base Rate plus two and one quarter percent (2.25%) with respect to Domestic Rate Loans and (b) the sum of the LIBOR Rate plus three and one-half percent (3.50%) with respect to LIBOR Rate Loans.

The repayment terms of the Term Loan provided for in the Twelfth Amendment consist of sixty (60) consecutive monthly principal installments, the first fifty-nine (59) of which shall be in the amount of \$123,133 commencing on the first business day of July, 2016, and continuing on the first business day of each month thereafter, with a sixty (60th) and final payment of any unpaid balance of principal and interest payable on the last business day of June, 2021. Under the terms of the Loan Facility, as amended, the revolving loan now bears interest at (a) the sum of the Alternate Base Rate plus one and three-quarters of one percent (1.75%) with respect to Domestic Rate Loans; and (b) the sum of the LIBOR Rate plus four and one-half of one percent (4.50%) with respect to LIBOR Rate Loan.

At the closing of the Twelfth Amendment the Company paid \$1,500,000 to reduce the outstanding excess under the revolving loan from \$12,500,000 to \$11,000,000. It also agreed that the excess advances will be paid down by \$100,000 each week commencing the second week after the closing of the Twelfth Amendment. The outstanding excess under the revolving loan is \$7,019,000 at September 30, 2016.

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

The terms of the Loan Facility require that among other things, the Company maintain a specified Fixed Charge Coverage Ratio and maintain a minimum EBITDA. In addition, the Company is limited in the amount of Capital Expenditures it can make. The Company is also limited to the amount of dividends it can pay its shareholders as defined in the Loan Facility. As of December 31, 2015, the Company was not in compliance with the Fixed Charge Coverage Ratio covenant. As of December 31, 2015, the Company was in compliance with all other terms of the Loan Facility. The failure to maintain the requisite Fixed Charge Coverage Ratio constitutes a default under the Loan Facility and PNC at its option may give notice to the Company that all amounts under the Loan Facility are immediately due and payable consequently, all amounts due under the Term Loans are also classified as current. For the three months ended September 30, 2016, PNC has excluded the Fixed Coverage Charge Ratio requirement. As of September 30, 2016, the Company was not in compliance with the minimum EBITDA requirement. The Company has requested a waiver from PNC for the failure to meet the minimum EBITDA covenant. Because the revolving loans contain a subjective acceleration clause which could permit PNC to require repayment prior to maturity, all of the loans outstanding with PNC are classified with the current portion of notes and capital lease obligations.

Each day, the Company's cash collections are swept directly by the bank to reduce the revolving loans and the Company then borrows according to a borrowing base formula. The Company's receivables are payable directly into a lockbox controlled by PNC (subject to the terms of the Loan Facility). PNC may use some elements of subjective business judgment in determining whether a material adverse change has occurred in the Company's condition, results of operations, assets, business, properties or prospects allowing it to demand repayment of the Loan Facility.

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As of September 30, 2016, the scheduled future minimum principal payments for the term loans are as follows, however as discussed above, the balance of the term loans have been classified as current:

For the twelve months ending	Amount
For the 12 Months Ended 9/30/17	\$ 1,478,000
For the 12 Months Ended 9/31/18	1,478,000
For the 12 Months Ended 9/31/19	1,478,000
For the 12 Months Ended 9/31/20	1,478,000
For the 12 Months Ended 9/31/21	1,107,000
PNC Term Loan payable	7,019,000
Less: Current portion	(7,019,000)
Long-term portion	\$ -

Capitalized Lease Obligations

The Company is committed under several capital leases for property and equipment. Each equipment lease has a bargain purchase option exercisable at the termination of the lease. The present value of the minimum lease payments required under the property lease is greater than 90% of the fair value of the asset at acquisition. Capital lease obligations totaled \$6,206,000 and \$5,018,000 as of September 30, 2016 and December 31, 2015, respectively, with various interest rates ranging from approximately 4% to 14%.

As of September 30, 2016, the aggregate future minimum lease payments, including imputed interest, with remaining terms of greater than one year are as follows:

For the twelve months ending	Amount
For the 12 Months Ended 9/30/2017	\$ 1,599,000
For the 12 Months Ended 9/30/2018	1,602,000
For the 12 Months Ended 9/30/2019	1,431,000
For the 12 Months Ended 9/30/2020	952,000
For the 12 Months Ended 9/30/2021	218,000
Thereafter	2,012,000
Total future minimum lease payments	7,814,000
Less: imputed interest	(1,608,000)
Less: current portion	(1,265,000)
Total Long Term Portion	\$ 4,941,000

Related Party Notes Payable

On September 8, 2015, the Company issued a promissory note (the "Taglich Note A") to Michael Taglich in the principal amount of \$350,000. The Taglich Note A bore interest at the rate of 4% per annum. The Company's obligation under the Taglich Note A was subordinated to its indebtedness to PNC.

On April 8, 2016, the Company issued a promissory note (the "Taglich Note B") to Michael Taglich in the principal amount of \$350,000. The Taglich Note B bore interest at the rate of 7% per annum. The Company's obligation under the Taglich Note B was subordinated to its indebtedness to PNC.

On April 8, 2016, the Company issued a promissory note (the "Taglich Note C") to Robert Taglich in the principal amount of \$350,000. The Taglich Note C bore interest at the rate of 7% per annum. The Company's obligation under the Taglich Note C was subordinated to its indebtedness to PNC.

On May 6, 2016, the Company issued a promissory note (the "Taglich Note D") to Michael Taglich in the principal amount of \$400,000. The Taglich Note D bore interest at the rate of 7% per annum. The Company's obligation under the Taglich Note D was subordinated to its indebtedness to PNC.

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On May 6, 2016, the Company issued a promissory note (the "Taglich Note E") to Robert Taglich in the principal amount of \$300,000. The Taglich Note E bore interest at the rate of 7% per annum. The Company's obligation under the Taglich Note E was subordinated to its indebtedness to PNC.

On May 25, 2016, the Company issued 110,000 and 65,000 shares of Series A Preferred Stock to Michael Taglich and Robert Taglich, respectively upon surrender of Taglich Notes A – E, in the aggregate principal of \$1,100,000 and \$650,000, respectively.

On August 1, 2016, the Company issued a promissory note (the "Taglich Note F") to Michael Taglich, in the principal amount of \$1,000,000. The Taglich Note F bore interest at the rate of 7% per annum. The Company's obligation under the Taglich Note F was subordinated to its indebtedness to PNC.

On August 4, 2016, the Company issued a promissory note (the "Taglich Note G") to Michael Taglich, in the principal amount of 500,000. The Taglich Note G bore interest at the rate of 7% per annum. The Company's obligation under the Taglich Note G was subordinated to its indebtedness to PNC.

On August 19, 2016 the Company issued to Michael Taglich a Note in the principal amount of \$1,520,703, together with Warrants to purchase 61,817 shares of common stock, upon surrender for cancellation of Taglich Notes F & G in the aggregate principal amount of \$1,500,000, together with accrued interest thereon and on notes previously exchanged for Series A Preferred Stock of \$20,703. In addition, the Company issued to Robert Taglich a Note in the principal amount of \$4,373, together with Warrants to purchase 177 shares of common stock, in consideration of the forgiveness of interest of \$4,373 accrued on notes previously exchanged for Series A Preferred Stock.

On November 10, 2016, one of the principal stockholders of the Company loaned the Company \$1,000,000. The terms of this loan have yet to be determined.

12% Subordinated Convertible Notes

On August 19, 2016, the Company entered into a Placement Agency Agreement with Taglich Brothers, Inc., as placement agent (the "Placement Agent"), pursuant to which the Placement Agent agreed to offer on behalf of the Company, on a best efforts basis, up to \$4,250,000 of the Company's 12% Subordinated Convertible Notes due December 31, 2017 (the "Notes") to accredited investors (the "Offering"), together with five-year warrants to purchase 4,065 shares of common stock (the "Warrants") for each \$100,000 principal amount of Notes purchased, in a private placement exempt from the registration requirements of the Securities Act of 1933, as amended (the "Securities Act").

The Notes are convertible, at the option of the holders, into shares of the Company's common stock at an initial conversion price of \$4.92 per share, subject to adjustment for certain events. The Notes are automatically convertible into shares of the Company's Series A Convertible Preferred Stock ("Series A Preferred Stock") at a price of \$10.00 per share, the stated value of the Series A Preferred Stock, upon the filing of a certificate of amendment to the Company's Articles of Incorporation increasing the number of shares of Series A Preferred Stock so that a sufficient number of shares are available for issuance upon conversion of the Notes and for issuance in lieu of payment of cash dividends (the "Certificate of Amendment") in accordance with the provisions of the certificate of designation authorizing the issuance of the Series A Preferred Stock. The amendment is subject to the approval of the Company's stockholders. The Company will submit the amendment to its stockholders for their approval at its 2016 Annual Meeting of Stockholders, which it expects to hold in the fourth quarter of 2016.

Under the terms of the Placement Agency Agreement, the Placement Agent is entitled to a placement agent fee equal to 7% of the gross proceeds of the offering, five year warrants to purchase 8% of the number of shares of the Company's common stock issuable upon conversion of the Notes at an exercise price of \$6.15 per share, equal to 125% of the initial conversion price per share of the Notes, and reimbursement for its actual out-of-pocket expenses not to exceed in the aggregate \$25,000.

In August 2016, the Company issued and sold a total of \$2,720,000 principal amount of the Notes, together with Warrants to purchase an aggregate of 110,556 shares of common stock, yielding net proceeds to the Company of approximately \$2,422,000, pursuant to a Securities Purchase Agreements with accredited investors. The Company also issued to Michael Taglich a Note in the principal amount of \$1,520,703, together with Warrants to purchase 61,817 shares of common stock, upon surrender for cancellation of Taglich Notes F and G in the aggregate principal amount of \$1,500,000, together with accrued interest thereon and on notes previously exchanged for Series A Preferred Stock of \$20,703. In addition, the Company issued to Robert Taglich a Note in the principal amount of \$4,373, together with Warrants to purchase 179 shares of common stock, in consideration of the forgiveness of interest of \$4,373 accrued on notes previously exchanged for Series A Preferred Stock.

The Warrants including those issued to the placement agent are classified within stockholders' equity, pursuant to ASC 480, Distinguishing Liabilities from Equity and ASC 815-40, Derivatives and Hedging: Contracts in Own Equity. The Notes contain a contingent put that results in early settlement of the Notes upon the filing of a certificate of amendment to the Company's Articles of Incorporation, increasing the number of shares of Series A Preferred Stock

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so that a sufficient number of shares are available for issuance upon conversion of the Notes. The embedded put feature is required to be separately measured at fair value with changes in value recognized in the statement of operations, pursuant to ASC 815-15, "Derivatives and Hedging: Embedded Derivatives", as the put feature is not clearly and closely related to the convertible promissory note.

The proceeds received upon issuing the Notes and Warrants was allocated to each instrument on a relative fair value basis. The initial fair value of the Warrants was determined using the Black Scholes Merton valuation model with the following assumptions: expected term of 5 years; risk free interest rate of 1.2%; and volatility of 90%. The allocated value of the Notes was further reduced for the initial fair value of the embedded put of approximately \$755,000. The resulting discount to the Notes, including the allocated transactions costs, is amortized to interest expense using the effective interest method over the term of the Notes.

Note 8. STOCKHOLDERS' EQUITY

Preferred Stock Offering

On May 25, 2016, the Company, entered into a Placement Agency Agreement (the "Agreement") with Craig-Hallum Capital Group LLC and Taglich Brothers, Inc., as placement agents (the "Placement Agents"), pursuant to which the Placement Agents agreed to offer on behalf of the Company, on a best efforts basis, up to \$7,000,000 of the Company's securities, (the "Offering"), in a private placement exempt from the registration requirements of the Securities Act of 1933.

Pursuant to the Agreement on May 25, 2016, and June 1, 2016, the Company completed a private placement of 700,000 shares of its Series A Convertible Stock (the "Series A Preferred Stock") from which it derived gross proceeds of \$5,250,000, net of \$1,750,000 of principal amount of the Company's promissory notes exchanged by Michael Taglich and Robert Taglich for shares of Series A Preferred Stock. The shares of Series A Preferred Stock have a stated value of \$10.00 per share ("Stated Value") and are initially convertible into shares of Common Stock at a price of \$4.92 per share (subject to adjustment upon the occurrence of certain events). In connection with the placement the Company incurred approximately \$606,000 of direct offering costs and \$57,000 in legal expenses and granted to the Placement Agents warrants to purchase 8% of the number of shares of the Company's common stock (113,822) issuable upon conversion of the Series A Preferred Stock sold in the offering (the "Placement Agent Warrants").

The Placement Agent Warrants are exercisable in whole or in part, at an initial exercise price per share of \$6.15, and are exercisable for cash or on a cashless basis for a period commencing on November 26, 2016 and expiring on May 26, 2021. The exercise price and number of shares of common stock issuable upon the exercise of the Placement Agent Warrants are subject to adjustment for stock dividends, splits, combinations and similar events.

Dividends on the Series A Preferred Stock (the "Preferred Shares") are payable on a cumulative basis at an annual rate for the first two years after the date the Preferred Shares were issued (the "Original Issue Date") of 12% of the Stated Value per share and thereafter at the annual rate of 16% of the Stated Value per share. Dividends are payable on the fifteenth day of March, June, September and December of each year, commencing on September 15, 2016. The Company may pay dividends in cash or in additional Preferred Shares ("PIK Shares"). If during the first two years after the Original Issue Date the Company fails to pay in respect of any dividend period a dividend at an annual rate of at least 8% of the Stated Value per share in cash, in addition to paying a sufficient number of PIK Shares so that the sum of the cash dividends and PIK Shares paid equals 12% per annum the Company will issue PIK Shares in an amount equal to the product of the proportion of the cash dividend not paid times 3% per annum. Thereafter if the Company fails to pay in respect of any dividend period a dividend at an annual rate of at least 10% of the Stated Value per share in cash, in addition to paying a sufficient number of PIK Shares so that the sum of the cash dividends and PIK Shares paid equals 16% per annum, the Company will issue PIK Shares in an amount equal to the product of the proportion of the cash dividend not paid times 3% per annum. If the Company pays any portion of the dividends payable during any dividend period in PIK Shares, it will not be permitted to declare or pay any cash dividends on its common stock during that dividend period.

Accordingly, we computed earned but undeclared preferred dividends at the stated rate of 12.0% through September 15, 2016, when the form of the dividend was announced and declared by our Board of Directors. Since the Board of Directors declared dividends in the form of PIK Shares for the dividend payment period ended September 15, 2016, the earned dividend was increased to 15% (from the 12% cash rate), as per the terms of the Series A Preferred Stock. The Company recognized the PIK dividend at the estimated fair value of the shares issued.

The Company recorded the issuance of 32,297 of PIK Shares during the three and nine months ended September 30, 2016 as a preferred dividend, with a fair value of \$300,000. Accordingly, accumulated deficit and Additional Paid In Capital were increased by that amount during the three and nine months ended September 30, 2016. The fair value was determined using the closing market price of the Company's common stock of \$4.57 per share on the date of issuance of the PIK Shares, taking into consideration that the Series A Preferred Shares were convertible into the common stock. For earnings per share purposes, for the three and nine months ended September 30, 2016, the fair value of the PIK Shares issued as a dividend was less than the amounts previously earned by \$23,000. At September 30, 2016 and December 31, 2015, the amounts of cumulative perpetual dividends earned and not declared on the Series A Preferred Stock were \$35,000 and \$0, based on the stated cash dividend rate of 12%, or \$0.05 and \$0 per Series A Preferred share, respectively.

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Under Nevada law and the terms of the Series A Preferred Stock, dividends are payable only when, as and if authorized and declared by the Company's board of directors. After payment of all liabilities and outstanding debt obligations, holders of Series A Preferred Stock are entitled to receive \$10.00 plus accrued and unpaid dividends prior to the payment of amounts available for distribution to holders of the Company's common stock upon the liquidation and dissolution of the Company.

Holders of Series A Preferred Stock may elect at any time to convert their Preferred Shares into shares of common stock at the conversion rate of 2.0325 shares of common stock for each Preferred Share, equivalent to an initial conversion price of approximately \$4.92 per share of common stock. The conversion rate and the corresponding conversion price will be subject to certain anti-dilution and other adjustments, including stock splits, distributions in respect of the common stock and in the event of certain fundamental transactions such as mergers and other business combinations.

The Company may at its option, at any time and from time to time after the market price of a share of common stock is in excess of \$9.84 for 30 consecutive trading days, cause all of the Preferred Shares to be converted into shares of common stock at the then-prevailing conversion rate, subject to the certain conditions set forth in the certificate of designations.

Commencing May 26, 2018, the Company may redeem all of the Preferred Shares for a redemption price of \$10.00, plus accrued and unpaid dividends.

Holders of Preferred Shares will vote on an as-converted basis, together with holders of common stock, as a single class, on the election of directors and all other matters presented to stockholders, except for matters as to which under applicable law and the certificate of designation a class vote of the holders of the Series A Preferred Stock is required. The Company may not, without the affirmative vote of the record holders of a majority of the then outstanding shares of the Series A Preferred Stock voting together as a single class (a) alter or change adversely the powers, preferences or rights given to the Series A Preferred Stock or alter or amend the Certificate of Designation authorizing the Series A Preferred Stock, (b) amend its articles of incorporation or other charter documents in any manner that adversely affects any rights of the holders, (c) increase the number of authorized shares of Series A Preferred Stock, unless such increase is necessary to pay PIK Dividends, (d) authorize a new series of preferred stock with dividend, liquidation or redemption rights senior or pari passu to the Series A Preferred Stock or (e) enter into any agreement with respect to any of the foregoing.

Common Stock Issuances

During the year ended December 31, 2015, the Company granted 52,000 shares of restricted common stock pursuant to an agreement in connection with the acquisition of Sterling. During the three and nine months ended September 30, 2016, 25,000 shares of that restricted stock has vested and is included in shares issued and outstanding. In addition, the Company issued an aggregate of 13,125 shares of common stock upon the exercise of options by certain of its directors.

Stock Options

On March 30, 2015, the Board of Directors adopted the Company's 2015 Equity Incentive Plan ("2015 Plan") which was approved by affirmative vote of the Company's stockholders on June 25, 2015. The Plan authorized the grant of rights with respect to up to 350,000 shares.

In June 2016, the Board of Directors adopted the Company's 2016 Equity Incentive Plan ("2016 Plan") which authorized the grant of rights with respect to up to 350,000 shares. The 2016 Plan will be submitted to stockholders for approval at the 2016 Annual Meeting of Stockholders.

During the three and nine months ended September 30, 2016 the Company granted options to purchase 0 and 138,000 shares of common stock to certain of its employees, respectively. The weighted average fair value of the granted options was estimated using the Black-Scholes option pricing model with the following assumptions: risk free interest rate of 1.36%; expected volatility factors of 25.00%; expected dividend yield of 0%; and estimated option term of 5 years.

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 9. INCOME TAXES

The provision for income taxes for the nine months ended September 30, 2016 and 2015 is set forth below:

	2016	2015
Current:		
Federal	-	117,000
State	13,000	14,000
Prior year (over)/under Accrual		
Federal	30,000	-
Total current expense	43,000	131,000
Deferred tax (benefit) expense	(2,145,000)	(650,000)
Total tax (benefit) expense	(2,102,000)	(519,000)

The components of net deferred tax assets are set forth below:

	September 30, 2016	December 31, 2015
Deferred Tax Assets		
Net operating losses	2,275,000	462,000
Bad debts	230,000	336,000
Accounts payable, accrued expenses and reserves	-	8,000
Inventory - 263A adjustment	1,035,000	919,000
Capitalized engineering costs	415,000	432,000
Deferred rent	413,000	410,000
Loss on extinguishment of debt	59,000	-
Deferred gain on sale of real estate	116,000	126,000
Lease impairment	-	-
Stock based compensation - options and restricted stock	132,000	79,000
Intangibles NTW	958,000	789,000
Capital loss carry forwards	-	-
Section 1231 loss carry forward	4,000	4,000
Inventory	725,000	680,000
Other	131,000	257,000
Total non-current deferred tax assets before valuation allowance	6,493,000	4,502,000
Valuation allowance	(4,000)	(4,000)
Total non-current deferred tax assets after valuation allowance	6,489,000	4,498,000
Deferred Tax Liabilities		
Property and equipment	(1,996,000)	(2,091,000)
Amortization - Welding Transaction	(270,000)	(313,000)
Amortization - NTW Goodwill	(16,000)	(13,000)
Amortization - AMK Goodwill	(29,000)	(18,000)
Total non-current deferred tax liabilities	(2,311,000)	(2,435,000)
Total Net Deferred Tax Assets	4,178,000	2,063,000

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

During the year ended December 31, 2015, the Company provided a valuation allowance on the deferred tax assets related to capital loss and section 1231 loss carryforwards. The valuation allowance at both September 30, 2016 and December 31, 2015 amounted to \$4,000. Management believes that the remainder of the net deferred tax assets are more likely than not to be realized.

The Company received a notice dated August 8, 2016 from the Internal Revenue Service for examination of its corporate tax return for the year ended December 31, 2014. Since the audit has not been completed, the Company cannot determine if any additional taxes, interest or penalties will be assessed.

Note 10. SEGMENT REPORTING

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

The Company follows ASC 280, which establishes standards for reporting information about operating segments in annual and interim financial statements, and requires that companies report financial and descriptive information about their reportable segments based on a management approach. ASC 280 also establishes standards for related disclosures about products and services, geographic areas and major customers.

The Company currently divides its operations into three operating segments: Complex Machining which consists of AIM and NTW; Aerostructures & Electronics which consists of WMI, WPI, Miller Stuart, Eur-Pac, ECC and Compac; and Turbine Engine Components which consists of AMK and Sterling.

The accounting policies of each segment are the same as those described in the Summary of Significant Accounting Policies. The Company evaluates performance based on revenue, gross profit contribution and assets employed.

AIR INDUSTRIES GROUP
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Financial information about the Company's operating segments for the three and nine months ended September 30, 2016 and 2015 are as follows:

	Three Months Ended September 30, 2016 (Unaudited)	2015 (Unaudited)	Nine Months Ended September 30, 2016 (Unaudited)	2015 (Unaudited)
COMPLEX MACHINING				
Net Sales	\$ 9,254,000	\$ 10,687,000	\$ 27,022,000	\$ 29,281,000
Gross Profit	1,476,000	2,568,000	5,898,000	6,886,000
Pre Tax (Loss) Income	(963,000)	549,000	(856,000)	733,000
Assets	54,159,000	47,811,000	54,159,000	47,811,000
AEROSTRUCTURES & ELECTRONICS				
Net Sales	3,738,000	7,408,000	14,939,000	19,468,000
Gross Profit	674,000	1,449,000	3,068,000	5,008,000
Pre Tax (Loss) Income	(893,000)	(126,000)	(1,832,000)	598,000
Assets	19,562,000	22,683,000	19,562,000	22,683,000
TURBINE ENGINE COMPONENTS				
Net Sales	2,718,000	2,981,000	8,296,000	8,195,000
Gross Profit	(153,000)	161,000	7,000	550,000
Pre Tax (Loss) Income	(1,248,000)	(812,000)	(2,900,000)	(2,010,000)
Assets	17,645,000	18,078,000	17,645,000	18,078,000
CORPORATE				
Net Sales	-	-	-	-
Gross Profit	-	-	-	-
Pre Tax (Loss) Income	(263,000)	-	(243,000)	-
Assets	574,000	596,000	574,000	596,000
CONSOLIDATED				
Net Sales	15,710,000	21,076,000	50,257,000	56,944,000
Gross Profit	1,997,000	4,178,000	8,973,000	12,444,000
Pre Tax (Loss) Income	(3,367,000)	(389,000)	(5,831,000)	(679,000)
Benefit from Income Taxes	1,320,000	726,000	2,102,000	519,000
Net Loss	(2,047,000)	337,000	(3,729,000)	(160,000)
Assets	\$ 91,940,000	\$ 89,168,000	\$ 91,940,000	\$ 89,168,000

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

The following discussion of our financial condition and results of operations should be read in conjunction with the unaudited consolidated financial statements and the notes to those statements included elsewhere in this Form 10-Q and with the audited consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2015 (the "2015 Form 10-K"). This discussion contains forward-looking statements that involve risks and uncertainties. You should specifically consider the various risk factors identified in the 2015 Form 10-K and our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2016 (the "Q2 2016 Form 10-Q") that could cause actual results to differ materially from those anticipated in these forward-looking statements.

Business Overview

We are an aerospace company operating primarily in the defense industry, though the proportion of our business represented by the commercial and industrial sector is increasing. We manufacture and design structural parts and assemblies that focus on flight safety, including landing gear, arresting gear, engine mounts, flight controls, throttle quadrants, and other components. We also provide sheet metal fabrication of aerostructures, tube bending, welding and kitting services. Our Turbine Engine Components segment makes components and provides services for jet engines and ground-power turbines. Our products are currently deployed on a wide range of high profile military and commercial aircraft including Sikorsky's UH-60 Blackhawk and CH-47 Chinook helicopters, Lockheed Martin's F-35 Joint Strike Fighter, Northrop Grumman's E2D Hawkeye, the US Navy F-18 and USAF F-16 fighter aircraft, Boeing's 777 and Airbus' 380 commercial airliners. Our Turbine Engine segment makes components for jet engines that are used on the USAF F-15 and F-16, the Airbus A-330 and A-380, and the Boeing 777, in addition to a number of ground-power turbine applications.

Air Industries Machining, Corp. ("AIM") became a public company in 2005 when its net sales were approximately \$30 million. AIM has manufactured components and subassemblies for the defense and commercial aerospace industry for over 45 years and has established long-term relationships with leading defense and aerospace manufacturers. Since becoming public, we have completed a series of acquisitions of defense aerospace and recently commercial aerospace businesses which have enabled us to broaden the range of products and services beyond those which were provided by AIM. For example, where AIM was primarily a machine shop, as a result of acquisitions, Air Industries Group now has capabilities and expertise in metal fabrication, welding and tube bending; the production of electromechanical systems, harness and cable assemblies; the fabrication of electronic equipment and printed circuit boards; the machining of turbine engine components, and the assembly of packages or "kits" containing supplies for all branches of the United States Defense Department, including ordnance parts, hose assemblies, hydraulic, mechanical and electrical assemblies.

In March 2015 we acquired the Sterling Engineering Corporation ("Sterling"). Sterling provides complex machining services and its business is concentrated with aircraft jet engine and ground turbine manufacturers. Sterling's results are reported as part of our Turbine Engine Components segment.

In September 2015 we acquired the business and operations of Compac Development Corporation ("Compac") in an asset acquisition. Compac specializes in the manufacture of RFI/EMI (Radio Frequency Interference – Electro-Magnetic Interference) shielded enclosures for electronic components. Its results are reported as part of our Aerostructures & Electronics segment.

The aerospace market is highly competitive in both the defense and commercial sectors and we face intense competition in all areas of our business. Nearly all of our revenues are derived by producing products to customer specifications after being awarded a contract through a competitive bidding process. As the commercial aerospace and defense industries continue to consolidate and major contractors seek to streamline supply chains by buying more complete sub-assemblies from fewer suppliers, we have sought to remain competitive not only by providing cost-effective world class service but also by increasing our ability to produce more complex and complete assemblies for our customers.

Our ability to operate profitably is determined by our ability to win new contracts and renewals of existing contracts, and then fulfill these contracts on a timely basis at costs that enable us to generate a profit based upon the agreed upon contract price. Winning a contract generally requires that we submit a bid containing a fixed price for the product or products covered by the contract for an agreed upon period of time. Thus, when submitting bids, we are required to estimate our future costs of production and, since we often rely upon subcontractors, the prices we can obtain from our subcontractors.

While our revenues are largely determined by the number of contracts we are awarded, the volume of product delivered and price of product under each contract, our costs are determined by a number of factors. The principal factors impacting our costs are the cost of materials and supplies, labor, financing and the efficiency at which we can produce our products. The cost of materials used in the aerospace industry is highly volatile. In addition, the market for the skilled labor we require to operate our plants is highly competitive. The profit margin of the various products we sell varies based upon a number of factors, including the complexity of the product, the intensity of the competition for such product and, in some cases, the ability to deliver replacement parts on short notice. Thus, in assessing our performance from one period to another, a reader must understand that changes in profit margin can be the result of shifts in the mix of products sold.

A very large percentage of the products we produce are used on military as opposed to civilian aircraft. These products can be replacements parts for aircraft already in the fleet of the armed services or for the production of new aircraft. Reductions to the Defense Department budget and decreased usage of aircraft by the military have reduced the demand for both new production and replacement spares. This has reduced our sales, particularly in our complex machining segment. In response to the reduction in military sales, we are focusing greater efforts on the civilian aircraft market though we still remain heavily dependent upon the military for an overwhelming portion of our revenues.

Segment Data

We follow Financial Accounting Standards Board ("FASB") ASC 280, "Segment Reporting" ("ASC 280"), which establishes standards for reporting information about operating segments in annual and interim financial statements, and requires that companies report financial and descriptive information about their reportable segments based on a management approach. ASC 280 also establishes standards for related disclosures about products and services, geographic areas and major customers.

We currently divide our operations into three operating segments: Complex Machining; Aerostructures & Electronics; and Turbine Engine Components. We separately report our corporate overhead (which was comprised of certain operating costs that were not directly attributable to a particular segment). Effective January 1, 2015, all operating costs are allocated to the Company's three operating segments. As our businesses continue to develop and evolve, and we acquire additional companies, we may deem it appropriate to reallocate our companies into different operating segments and, once we achieve sufficient integration among our businesses, report as a unified company.

The accounting policies of each of the segments are the same as those described in the Summary of Significant Accounting Policies. We evaluate performance based on revenue, gross profit contribution and assets employed.

Results of Operations

The following discussion of our results of operations constitutes management's review of the factors that affected our financial and operating performance for the three and nine months ended September 30, 2016 and 2015. This discussion should be read in conjunction with the financial statements and notes thereto contained elsewhere in this report. The results of operations of the businesses we have acquired are included in our financial results from their respective dates of acquisition.

Selected Financial Information:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016 (Unaudited)	2015 (Unaudited)	2016 (Unaudited)	2015 (Unaudited)
Net Sales	\$ 15,710,000	\$ 21,076,000	\$ 50,257,000	\$ 56,944,000
Cost of Sales	13,713,000	16,898,000	41,284,000	44,500,000
Gross Profit	1,997,000	4,178,000	8,973,000	12,444,000
Operating Expenses and interest costs	5,196,000	4,603,000	14,667,000	13,221,000
Other Income, Net	4,000	36,000	35,000	98,000
Benefit from Income Taxes	1,320,000	726,000	2,102,000	519,000
Net (Loss) Income	(2,047,000)	337,000	(3,729,000)	(160,000)

Balance Sheet Data:

	<u>September 30,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
	<u>(Unaudited)</u>	<u>(Unaudited)</u>
Cash and Cash Equivalents	\$ 1,297,000	\$ 529,000
Working Capital	5,963,000	441,000
Total Assets	91,940,000	88,250,000
Total Stockholders' Equity	32,266,000	28,805,000

The following sets forth the results of operations for each of our segments individually and on a consolidated basis for the periods indicated:

	<u>Three Months Ended September 30,</u> <u>2016</u>	<u>2015</u>	<u>Nine Months Ended September 30,</u> <u>2016</u>	<u>2015</u>
	<u>(Unaudited)</u>	<u>(Unaudited)</u>	<u>(Unaudited)</u>	<u>(Unaudited)</u>
COMPLEX MACHINING				
Net Sales	\$ 9,254,000	\$ 10,687,000	\$ 27,022,000	\$ 29,281,000
Gross Profit	1,476,000	2,568,000	5,898,000	6,886,000
Pre Tax (Loss) Income	(963,000)	549,000	(856,000)	733,000
Assets	54,159,000	47,811,000	54,159,000	47,811,000
AEROSTRUCTURES & ELECTRONICS				
Net Sales	3,738,000	7,408,000	14,939,000	19,468,000
Gross Profit	674,000	1,449,000	3,068,000	5,008,000
Pre Tax (Loss) Income	(893,000)	(126,000)	(1,832,000)	598,000
Assets	19,562,000	22,683,000	19,562,000	22,683,000
TURBINE ENGINE COMPONENTS				
Net Sales	2,718,000	2,981,000	8,296,000	8,195,000
Gross Profit	(153,000)	161,000	7,000	550,000
Pre Tax Loss (Loss) Income	(1,248,000)	(812,000)	(2,901,000)	(2,010,000)
Assets	17,645,000	18,078,000	17,645,000	18,078,000
CORPORATE				
Net Sales	-	-	-	-
Gross Profit	-	-	-	-
Pre Tax (Loss) Income	(263,000)	-	(243,000)	-
Assets	574,000	596,000	574,000	596,000
CONSOLIDATED				
Net Sales	15,710,000	21,076,000	50,257,000	56,944,000
Gross Profit	1,997,000	4,178,000	8,973,000	12,444,000
Pre Tax (Loss) Income	(3,367,000)	(389,000)	(5,831,000)	(679,000)
Benefit from Income Taxes	1,320,000	726,000	2,102,000	519,000
Net Loss	(2,047,000)	337,000	(3,729,000)	(160,000)
Assets	\$ 91,940,000	\$ 89,168,000	\$ 91,940,000	\$ 89,168,000

Results of Operations for the three months ended September 30, 2016

Consolidated net sales for the three months ended September 30, 2016 were approximately \$15,710,000, a decrease of (\$5,366,000), or (25.5%), compared with \$21,076,000 for the three months ended September 30, 2015. The decrease in sales resulted from decreases in sales in all of our segments. Sales decreased (\$1,433,000) at Complex Machining, (\$3,670,000) at Aerostructures & Electronics and (\$263,000) in Turbine Engine Components.

- The decrease in Complex Machining resulted primarily from a decrease in orders and deliveries at Air Industries Machining partially offset by increases at Nassau Tool Works.
- The decline at Aerostructures & Electronics reflected decreased customer demand together with operational and execution issues.
- The modest decline in the Turbine Engine Components segment reflected gains at AMK offset by decreases at Sterling Engineering. The decline at Sterling reflects the fact that during the quarter a high percentage of its operations were devoted to new products under development and not yet in full rate production.

As indicated in the table below, one customer represented 14.2% and four customers represented 55.3% of total sales for the three months ended September 30, 2016 and 2015, respectively.

Customer	Percentage of Sales	
	2016 (Unaudited)	2015 (Unaudited)
Sikorsky Aircraft	14.2	18.8
Goodrich Landing Gear	*	15.3
US DoD	*	11.1
Northrop Grumman Corporation	*	10.1

*Customer was less than 10% of sales for the quarter ended September 30, 2016

Sikorsky Aircraft and Goodrich Landing Gear Systems are units of United Technologies Corporation.

Gross Profit:

Consolidated gross profit from operations for the three months ended September 30, 2016 was \$1,997,000 a decrease of approximately (\$2,181,000), or (52.2%), as compared to gross profit of \$4,178,000 for the three months ended September 30, 2015. Consolidated gross profit as a percentage of sales was 12.7% and 19.8% for the three months ended September 30, 2016 and 2015, respectively.

- Gross profit at Complex Machining segment decreased by \$1,092,000 for the three months ended September 30, 2016 as a result of lower sales and decreased absorption of factory overhead particularly at Air Industries Machining.
- Gross Profit at Aerostructures & Electronics segment decreased by \$775,000 for the three months ended September 30, 2016, resulting from lower sales and under absorption of factory overhead.
- Gross profit at Turbine Engine Component segment declined by \$314,000 for the three months ended September 30, 2016 due to lower revenues at Sterling Engineering resulting in under absorption of factory overhead. Gross profit at AMK increased slightly.

Operating Expenses:

Consolidated Operating Expenses for the three months ended September 30, 2016 were \$4,302,000 and increased by \$150,000, or 3.6%, compared to \$4,152,000 for the three months ended September 30, 2015. Operating costs increased due to increased legal and accounting expense resulting from several equity capital placements and amendments to our loan agreements.

Interest and financing costs for the three months ended September 30, 2016 were approximately \$894,000 an increase of approximately \$443,000, or 98.2% compared to \$451,000 for the three months ended September 30, 2015 reflecting both an increase in the amount of our debt and the interest rate payable as a result of the modifications of our Loan Facility.

Loss before income taxes for the three months ended September 30, 2016 was (\$3,367,000), an increase of \$2,978,000 compared to loss before income taxes of (\$389,000) for the three months ended September 30, 2015.

The Company recognized a benefit from taxes of \$1,297,000 for three months ended September 30, 2016 compared to a benefit from taxes of approximately \$726,000 for three months ended September 30, 2015, a difference of \$571,000.

Net loss for the three months ended September 30, 2016 was (\$2,047,000) a decrease of (\$2,384,000), or 707.4%, compared to net gain of \$337,000 for the three months ended September 30, 2015 for the reasons discussed above.

Results of Operations for the nine months ended September 30, 2016

Consolidated net sales for the nine months ended September 30, 2016 were approximately \$50,257,000, a decrease of (\$6,687,000), or (11.7%), compared with \$56,944,000 for the nine months ended September 30, 2015. A slight \$101,000 increase in sales during the nine months of \$8,296,000 or 1.2% at our Turbine & Engine segment was more than offset by sales decreases of (\$2,259,000) or (7.7%) at Complex Machining and (\$4,529,000) or 23.3% at Aerostructures & Electronics.

- The decrease at Complex Machining resulted primarily from a decrease in orders and deliveries at Air Industries Machining partially offset by increases at Nassau Tool Works.
- The decline at Aerostructures & Electronics resulted from declines in sales for all of its business units and reflected decreased customer demand together with operational and execution issues.
- The increase in the Turbine Engine Components segment reflected gains at both AMK and Sterling Engineering.

As indicated in the table below, four customers represented 53.3% and 62.1% of total sales for the nine months ended September 30, 2016 and 2015, respectively.

Customer	Percentage of Sales	
	2016	2015
	(Unaudited)	(Unaudited)
Sikorsky Aircraft	19.8	17.0
Goodrich Landing Gear	11.9	14.9
Northrop Grumman Corporation	10.9	17.3
US DoD	10.7	12.9

Gross Profit:

Consolidated gross profit from operations for the nine months ended September 30, 2016 was \$8,973,000 a decrease of approximately (\$3,471,000), or (27.9%), as compared to gross profit of \$12,444,000 for the nine months ended September 30, 2015. Consolidated gross profit as a percentage of sales was 17.9% and 21.9% for the nine months ended September 30, 2016 and 2015, respectively. The decline in gross profit reflects the decline in sales and the underabsorption of factory overhead.

- Gross profit at Complex Machining decreased by (\$988,000) for the nine months ended September 30, 2016 resulting from lower sales and under absorption of factory overhead.
- Gross Profit at Aerostructures & Electronics decreased by (\$1,940,000) for the nine months ended September 30, 2016 resulting from the absence of a biennial contract which generated significant revenues in 2015 and under absorption of factory overhead.
- Gross profit at our Turbine Engine Component segment decreased by (\$543,000) for the nine months ended September 30, 2016 due to decreased revenues at both AMK and Sterling Engineering.

Operating Expenses:

Consolidated Operating Expenses for the nine months ended September 30, 2016 totaled approximately \$12,896,000 and increased by \$1,016,000, or 8.6%, compared to \$11,880,000 for the nine months ended September 30, 2015.

Interest and financing costs for the nine months ended September 30, 2016 were approximately \$1,771,000 an increase of approximately \$430,000, or 32.1%, compared to \$1,341,000 for the nine months ended September 30, 2015. The increase in financing costs reflects the costs of raising capital, the increase in our outstanding debt and in the rates payable on our debt.

Loss before taxes for the nine months ended September 30, 2016 was (\$5,831,000), an increase in our loss of (\$5,152,000) or 759.1%, compared to a loss before taxes of (\$679,000) for the nine months ended September 30, 2015.

The Company recognized a benefit for income taxes of approximately \$2,102,000 for nine months ended September 30, 2016 compared to a benefit for taxes of approximately \$519,000 for nine months ended September 30, 2015, an increase of \$1,583,000 primarily from the increased net operating losses generated by the Company.

Net loss for the nine months ended September 30, 2016 was (\$3,729,000), a decrease in performance of (\$3,569,000), or 2,230.6%, compared to net loss of (\$160,000) for the nine months ended September 30, 2015. The decrease in net income results primarily from the impact of the losses incurred at each of our operating segments.

LIQUIDITY AND CAPITAL RESOURCES

We are highly leveraged and rely upon our ability to continue to borrow from PNC Bank N.A. ("PNC") to support operations and acquisitions. Substantially all of our assets are pledged as collateral under our existing loan agreements with PNC. Our Company is required to maintain a lockbox account with PNC, into which substantially all of our cash receipts are paid. If PNC were to cease lending, we would lack funds to continue our operations. Over the past twelve months we have also relied upon our ability to borrow money from certain stockholders and raise equity capital to support our operations. Should we continue to need to borrow funds from our principal stockholders or raise equity, there is no assurance that we will be able to do so or that the terms on which we borrow funds or raise equity will be favorable to us or our existing shareholders.

We have a credit facility with PNC (the "Loan Facility") secured by substantially all of our assets. The Loan Facility has been amended many times during its term. The Loan Facility was amended in June 2016 (the "Twelfth Amendment") and September 2016 (the "Thirteenth Amendment"). In connection with the Twelfth Amendment, we paid a fee of \$100,000 and reimbursed PNC for the fees and expenses of its counsel. The Twelfth Amendment provides for a \$33,000,000 revolving loan. In addition, in the Twelfth Amendment the four term loans (Term Loan A, Term Loan B, Term Loan C and Term Loan D) then outstanding were consolidated into a single term loan with the initial principal amount of \$7,387,854. Further, in the Twelfth Amendment we acknowledged that there were then outstanding excess advances under the revolver in the amount of \$12,500,000.

Under the terms of the Loan Facility, as amended, the revolving loan now bears interest at (a) the sum of the Alternate Base Rate plus one and three-quarters of one percent (1.75%) with respect to Domestic Rate Loans; and (b) the sum of the LIBOR Rate plus four and one-half of one percent (4.50%) with respect to LIBOR Rate Loans. The amount outstanding under the revolving loan, exclusive of the excess advance, was \$25,822,000 and \$29,604,000, as of September 30, 2016 and December 31, 2015, respectively.

The Loan Facility was further amended pursuant to the Thirteenth Amendment, to modify the advance rate with respect to our inventory to be the lesser of (i) 75% of the eligible inventory, an increase from 50%, and (ii) 90% of the liquidation value of the eligible inventory, an increase from 85%, subject to the inventory sublimit of \$12,500,000 and such reserves as PNC may deem proper. In addition, in the Thirteenth Amendment the lender waived any default resulting from our obligation to comply with the minimum EBITDA covenant for the period ended June 30, 2016, consented to the issuance of our 12% Subordinated Convertible Notes and the amendment to our Articles of Incorporation to increase the authorized number of shares of Preferred Stock and Series A Preferred Stock.

The repayment terms of Term Loan A had previously been amended in 2014 when the Company borrowed \$2,676,000, representing an additional \$1,328,000 and Term Loan A as amended was to be repaid in monthly installments of \$31,859 continuing until November 2016. On October 1, 2014, the Company borrowed \$3,500,000 under Term Loan B for the acquisition of AMK. Term Loan B was to be repaid in sixty consecutive monthly principal installments of \$58,333 continuing until November 2019. Prior to the Twelfth Amendment, Term Loans A and B bore interest at (a) the sum of the Alternate Base Rate plus one and three quarters of one percent (1.75%) with respect to Domestic Rate Loans and (b) the sum of the LIBOR Rate plus three percent (3.00%) with respect to LIBOR Rate Loans.

On December 31, 2014, we borrowed \$2,500,000 under Term Loan C to refinance the Seller Note and Mortgage of \$2,500,000 issued as part of the acquisition of AMK. Term Loan C was originally to be repaid in monthly installments of \$34,722 continuing until January 2021. Prior to the Twelfth Amendment, Term Loan C bore interest at (a) the sum of the Alternate Base Rate plus two percent (2.00%) with respect to Domestic Rate Loans and (b) the sum of the LIBOR Rate plus three and one-quarter percent (3.25%) with respect to LIBOR Rate Loans.

On March 9, 2015, we borrowed \$3,500,000 under Term Loan D for the acquisition of Sterling. Prior to the Twelfth Amendment, Term Loan D was to be repaid through twenty consecutive monthly installments of \$62,847 continuing until November 2016. Term Loan D bore interest at (a) the sum of the Alternate Base Rate plus two and one quarter percent (2.25%) with respect to Domestic Rate Loans and (b) the sum of the LIBOR Rate plus three and one-half percent (3.50%) with respect to LIBOR Rate Loans.

The repayment terms of the Term Loan provided for in the Twelfth Amendment consist of sixty (60) consecutive monthly principal installments, the first fifty-nine (59) of which shall be in the amount of \$123,133 commencing on the first business day of July, 2016, and continuing on the first business day of each month thereafter, with a sixty (60th) and final payment of any unpaid balance of principal and interest payable on the last business day of June, 2021. Under the terms of the Loan Facility, as amended, the revolving loan now bears interest at (a) the sum of the Alternate Base Rate plus one and three-quarters of one percent (1.75%) with respect to Domestic Rate Loans; and (b) the sum of the LIBOR Rate plus four and one-half of one percent (4.50%) with respect to LIBOR Rate Loan.

At the closing of the Twelfth Amendment we paid \$1,500,000 to reduce the outstanding excess under the revolving loan. It also agreed that to reduce the excess advances by \$100,000 each week commencing the second week after the closing of the Twelfth Amendment.

The terms of the Loan Facility require that, among other things, we maintain a specified Fixed Charge Coverage Ratio and maintain a minimum EBITDA. In addition, we are limited in the amount of Capital Expenditures we can make. We are also limited to the amount of dividends we can pay our shareholders as defined in the Loan Facility. As of December 31, 2015, we were not in compliance with the Fixed Charge Coverage Ratio covenant. As of December 31, 2015, we were in compliance with all other terms of the Loan Facility. The failure to maintain the requisite Fixed Charge Coverage Ratio constitutes a default under the Loan Facility and PNC at its option may give notice to us that all amounts under the Loan Facility are immediately due and payable. Consequently, all amounts due under the Term Loans are also classified as current. For the three months ended September 30, 2016, PNC has excluded the Fixed Coverage Charge Ratio requirement. As of September 30, 2016, we were not in compliance with the minimum EBITDA requirement. We have requested a waiver from PNC for the failure to meet the minimum EBITDA covenant.

As of September 30, 2016, our debt to PNC in the amount of \$32,841,000 consisted of the revolving credit note due to PNC in the amount of \$25,822,000, the term loans due to PNC in the amount of \$7,019,000, and capitalized lease obligations of \$6,206,000.

Subordinated Loans, Issuance of Preferred Stock and Note Offering

During the period September 2015 through May 2016, we borrowed an aggregate of \$1,750,000 from two of our principal stockholders. The September 2015 loan bore interest at the rate of 4% per annum and was to be paid on September 7, 2016. The other loans bore interest at the rate of 7% per annum and were to be repaid on June 30, 2016, or, if earlier, upon the sale of the Company's equity from which it derived proceeds of \$2,000,000. The indebtedness related to these loans was converted into a total of 175,000 shares of Series A Preferred Stock in connection the private placement discussed below.

On May 25, 2016, and June 1, 2016, we completed a private placement of 700,000 shares of our Series A Preferred Stock from which we derived gross proceeds of \$5,250,000, net of \$1,750,000 of principal amount of our promissory notes exchanged by Michael Taglich and Robert Taglich for shares of Series A Preferred Stock. The shares of Series A Preferred Stock have a stated value of \$10.00 per share and are initially convertible into shares of Common Stock at a price of \$4.92 per share (subject to adjustment upon the occurrence of certain events). In connection with the placement we incurred approximately \$606,000 of direct offering costs and \$57,000 in legal expenses and granted to the Placement Agents warrants to purchase 8% of the number of shares of our common stock (113,822 shares) issuable upon conversion of the Series A Preferred Stock sold in the offering. The warrants are exercisable in whole or in part, at an initial exercise price per share of \$6.15, and are exercisable for cash or on a cashless basis commencing on November 26, 2016 and expiring on May 26, 2021. The exercise price and number of shares of common stock issuable under the warrants are subject to adjustments for stock dividends, splits, combinations and similar events.

Of the proceeds generated by the sale of our Preferred Shares, \$1,500,000 was paid to PNC to reduce the amount outstanding under our Loan Facility.

In August 2016, we borrowed an aggregate of \$1,500,000 from one of our principal stockholders. The loans are evidenced by promissory notes bearing interest at the rate of 7% per annum and are to be repaid on December 31, 2016, or, if earlier, upon the sale of our equity securities from which we derived proceeds of \$2,000,000.

On September 1, 2016 we completed the private placement of \$2,720,000 principal amount of our 12% Subordinated Convertible Notes due December 31, 2017 (the "Notes"), together with Investor Warrants to purchase an aggregate of 110,658 shares of common stock, for a total purchase price of \$2,720,000. We issued the Notes since we did not have sufficient shares of preferred stock available. The Notes are automatically convertible into shares of Series A Preferred Stock at a price of \$10.00 per share, the stated value of the Series A Preferred Stock, upon the filing of an amendment to our charter increasing the number of authorized shares of Series A Preferred Stock. The Company received net proceeds of approximately \$2,319,800 from the sale of the Notes, which was used to pay down our indebtedness under the Loan Agreement and for working capital. The Company also issued to Michael Taglich a Note in the principal amount of \$1,520,713, together with Investor Warrants to purchase 61,817 shares of common stock, upon surrender for cancellation of promissory notes in the aggregate principal amount of \$1,500,000, together with accrued interest thereon and on notes previously exchanged for Series A Preferred Stock of \$20,713. In addition, we issued to Robert Taglich a Note in the principal amount of \$4,373, together with Investor Warrants to purchase 177 shares of Common Stock, in consideration of the forgiveness of interest of \$4,373 accrued on notes previously exchanged for Series A Preferred Stock.

As compensation for its services as placement agent for the offering, we paid Taglich Brothers a fee of \$295,400 and issued to Taglich Brothers five-year warrants to purchase 68,617 shares of Common Stock at an initial exercise price of \$6.15, subject to certain anti-dilution and other adjustments, including stock splits, distributions in respect of the common stock and in the event of certain fundamental transactions such as mergers and other business combinations.

On September 15, 2016, we issued 32,297 shares of Series A Preferred Stock in lieu of payment of cash dividends on the 700,000 shares of Series A Preferred Stock issued in the Preferred Stock Offering.

The issuance of the Notes in August 2016 increased our indebtedness by \$2,720,000 after giving effect to the retirement of a \$1,500,000 promissory note exchanged as a portion of the consideration for a Note in the principal amount of \$1,520,703. As a result of the automatic conversion of the Notes, the indebtedness represented by the Notes will be eliminated, but the number of outstanding shares of Series A Preferred Stock will increase from 700,000 shares to approximately 1,140,000 shares. The Notes, which are payable on December 31, 2018, bear interest at the rate of 12% per annum, the same nominal rate as dividends accrue on the Series A Preferred Stock through June 15, 2018. The dividend rate on the Series A Preferred Stock increases to 15% per annum if we issue PIK Shares in lieu of payment of cash dividends payable until June 15, 2018, and the number of outstanding shares of Series A Preferred Stock as of such date would increase to approximately 1,500,000 shares if we elected to pay all dividends due on the Series A Preferred Stock by issuing PIK Shares. The dividend rate on the Series A Preferred Stock increases to 16% per annum after June 2018, 19% per annum to the extent dividends are paid in PIK Shares.

Interest payable on the Notes and dividends payable in respect of the Series A Preferred Stock will reduce the amount of net income, if any, or increase the amount of net loss attributable to holders of common stock. While the issuance of PIK Shares in payment of all or a portion of the dividends payable in respect of any dividend period preserves our cash, the increase in the rate of dividend which must be paid when we choose to issue PIK Shares in lieu of cash dividends further reduces the amount of net income, if any, or increases the amount of net loss attributable to holders of common stock. In addition, the issuance of PIK Shares will dilute the interests of our common stockholders. Furthermore, under the terms of the Certificate of Designation authorizing the issuance of our Series A Preferred Stock, we are not permitted to declare or pay any cash dividends on our common stock during any dividend period if we pay all or a portion of the dividends on the Series A Preferred Stock in PIK Shares. Although holders of Series A Preferred Stock may convert their shares into common stock they are unlikely to convert if we are unable to pay cash dividends and the price of the common stock does not increase significantly above \$4.92 per share, the conversion price, for a sustained period. We have the right to redeem the Series A Preferred Stock after May 26, 2018 for a redemption price of \$10.00, plus accrued and unpaid dividends; however, we may not have sufficient cash available to effect such redemption.

Anticipated Uses of Cash

As a requirement of our Loan Facility substantially all of our cash receipts from operations are deposited into our lockbox account at PNC. These cash receipts are used to reduce our indebtedness under our revolving credit note and are then borrowed according to a borrowing base to support our operations. In addition, dividends on the Preferred Shares are payable on a cumulative basis at an annual rate for the first two years after the date the Preferred Shares were issued of 12% of the Stated Value per share and thereafter at the annual rate of 16% of the Stated Value per share. The Company may pay dividends in cash or in additional Preferred Shares ("PIK Shares"). If during the first two years after the date of issuance the Company fails to pay dividends in respect of any dividend period a dividend at an annual rate of at least 8% of the Stated Value per share in cash, in addition to paying a sufficient number of PIK Shares so that the sum of the cash dividends and PIK Shares paid equals 12% per annum the Company will issue PIK Shares in an amount equal to the product of the proportion of the cash dividend not paid times 3% per annum.

Cash Flow

The following table summarizes our net cash flow from operating, investing and financing activities for the periods indicated below:

	September 30, 2016 <u>(Unaudited)</u>	September 30, 2015 <u></u>
Cash provided by (used in)		
Operating activities	\$ (1,124,000)	\$ (1,449,000)
Investing activities	(314,000)	(7,772,000)
Financing activities	2,206,000	8,594,000
Net increase (decrease) in cash and cash equivalents	\$ 768,000	\$ (627,000)

Cash Provided By Operating Activities

Cash provided by operating activities primarily consists of our net income (loss) adjusted for certain non-cash items and changes to working capital.

For the nine months ended September 30, 2016, the net cash used in our operating activities of (\$1,124,000) was comprised of a net loss of (\$3,729,000), reduced by (\$2,145,000) due to changes in deferred income taxes, a loss on extinguishment of debt \$172,000, and \$184,000 related to amortization of convertible notes payable, offset by adjustments for non-cash items of \$4,535,000. Adjustments for non-cash items consisted primarily of depreciation of property and equipment of \$2,808,000, amortization of capitalized engineering costs, intangibles and other items of \$1,598,000, and non-cash compensation of \$126,000. These non-cash items were offset by (\$29,000) of deferred gain on the sale of real estate. The net decrease in operating assets was comprised of an increase in inventory of \$6,389,000, a decrease in accounts receivable of \$3,730,000 due to the timing of shipments to and cash receipts from customers, a decrease in prepaid expenses and other current assets of \$255,000, offset by an increase in deposits and other assets of (\$199,000). The net increase in operating liabilities was comprised of increases in accounts payable and accrued expenses of \$2,356,000 due to the timing of the receipt and payment of invoices, a decrease in income taxes payable of \$14,000, and increases in deferred rent of \$10,000 and deferred revenue of \$112,000.

Cash Used in Investing Activities

Cash used in investing activities consists of capital expenditures for property and equipment, capitalized engineering costs and the cash payments for the businesses we acquired. A description of capitalized engineering costs can be found below and in Note 3 Summary of Significant Accounting Policies in our Consolidated Financial Statements for the year ended December 31, 2015.

For the nine months ended September 30, 2016, cash used by investing activities was (\$314,000). This was comprised of (\$644,000) of capitalized engineering costs, (\$1,341,000) used for the purchase of property and equipment, offset by the proceeds of the sale of fixed assets of \$1,671,000.

Cash Provided By (Used In) Financing Activities

Cash provided by or used in financing activities primarily consists of the proceeds of the sale of our equity securities, borrowings and repayments under our credit facilities with our senior lender, increases in and repayments of capital lease obligations and other notes payable, and dividend payments.

For the nine months ended September 30, 2016, cash provided by financing activities was \$2,206,000. This was comprised of the net proceeds from the issuance of notes payable of \$5,620,000 and the net proceeds from the issuance of preferred stock of \$5,250,000, offset in part by repayments of (\$6,596,000) on our revolving line of credit and term loans and (\$908,000) on our capital lease obligations, (\$199,000) of deferred financing costs, and expenses of (\$663,000) related to the issuances of preferred stock and (\$298,000) for the issuance of convertible debt.

OFF-BALANCE SHEET ARRANGEMENTS

We did not have any off-balance sheet arrangements as of September 30, 2016.

Critical Accounting Policies

We have identified the policies below as critical to our business operations and the understanding of our financial results.

Inventory Valuation

For interim reporting, the Company computes its inventory using the "gross profit" method for some subsidiaries.

For annual reporting, the Company values inventory at the lower of cost on a first-in-first-out basis or market.

We generally purchase raw materials and supplies uniquely for the production of larger more complex parts, such as landing gear, only when non-cancellable contracts for orders have been received for finished goods. We occasionally produce products, in excess of purchase order quantities in anticipation of future purchase order demand. Historically this excess has been used in fulfilling future purchase orders. We purchase supplies and materials useful in a variety of products as deemed necessary even though orders have not been received. The Company periodically evaluates inventory items that are not secured by purchase orders and establishes reserves for obsolescence accordingly. The Company also reserves for excess quantities, slow-moving goods, and for other impairments of value.

The Company presents inventory net of progress billings in accordance with the specified contractual arrangements with the United States Government, which results in the transfer of title of the related inventory from the Company to the United States Government, when such progress payments are received.

Capitalized Engineering Costs

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

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

Revenue Recognition

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

The Company recognizes certain revenues under a bill and hold arrangement with two of its large customers. For any requested bill and hold arrangement, the Company makes an evaluation as to whether the bill and hold arrangement qualifies for revenue recognition. The customer must initiate the request for the bill and hold arrangement. The customer must have made this request in writing in addition to their fixed commitment to purchase the item. The risk of ownership has passed to the customer, payment terms are not modified and payment will be made as if the goods had shipped.

Income Taxes

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

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

Stock-Based Compensation

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

Goodwill

Goodwill represents the excess of the acquisition cost of businesses over the fair value of the identifiable net assets acquired. Goodwill is not amortized, but is tested at least annually for impairment, or if circumstances change that will more likely than not reduce the fair value of the reporting unit below its carrying amount.

The Company accounts for the impairment of goodwill under the provisions of ASU 2011-08 ("ASU 2011-08"), "Intangibles Goodwill and Other (Topic 350): Testing Goodwill for Impairment." ASU 2011-08 updated the guidance on the periodic testing of goodwill for impairment. The updated guidance gives companies the option to perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount.

The Company performs impairment testing for goodwill annually, or more frequently when indicators of impairment exist, using a three-step approach. Step "zero" is a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. Step one compares the fair value of the net assets of the relevant reporting unit (calculated using a discounted cash flow method) to its carrying value, a second step is performed to compute the amount of the impairment. In this process, a fair value for goodwill is estimated, based in part on the fair value of the operations, and is compared to its carrying value. The shortfall of the fair value below carrying value represents the amount of goodwill impairment.

Long-Lived and Intangible Assets

Identifiable intangible assets are amortized using the straight-line method over the period of expected benefit. Long-lived assets and intangible assets subject to amortization to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the related carrying amount may be impaired. The Company records an impairment loss if the undiscounted future cash flows are found to be less than the carrying amount of the asset. If an impairment loss has occurred, a charge is recorded to reduce the carrying amount of the asset to fair value. There has been no impairment as of September 30, 2016 and December 31, 2015.

Recently Issued Accounting Pronouncements

In January 2016, the FASB issued ASU 2016-01, “Recognition and Measurement of Financial Assets and Financial Liabilities (Subtopic 825-10)” (“ASU 2016-01”). The main objective of ASU 2016-01 is enhancing the reporting model for financial instruments to provide users of financial statements with more decision-useful information. The amendments address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. ASU 2016-01 is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The Company does not expect the adoption of this amended to have a significant impact on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842)” (“ASU 2016-02”). The main objective of ASU 2016-02 is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. To meet that objective, the FASB is amending the FASB Accounting Standards Codification and creating Topic 842, Leases. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Company does not expect the adoption of this amended to have a significant impact on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, “Compensation—Stock Compensation (Topic 718) Improvements to Employee Share-Based Payment” (“ASU 2016-09”). ASU 2016-09 is part of the FASB Simplification Initiative. The objective of the Simplification Initiative is to identify, evaluate, and improve areas of generally accepted accounting principles for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to users of financial statements. ASU 2016-09 will affect all entities that issue share-based payment awards to their employees. The areas for simplification involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. The Company does not expect the adoption of this amended to have a significant impact on its consolidated financial statements.

In April 2016, the FASB issued ASU 2016-10 “Revenue from Contracts with Customers (Topic 606)” (“ASU 2016-10”). The core principle of the guidance in Topic 606 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments in ASU 2016-10 affect the guidance in ASU 2014-09, “Revenue from Contracts with Customers”, which is not yet effective. The effective date and transition requirements of ASU 2016-10 are the same as the effective date and transition requirements of ASU 2014-09. They are effective prospectively for reporting periods beginning after December 15, 2017 and early adoption is not permitted. The Company is currently assessing the impact of the adoption of these amendments on its consolidated financial statements.

In May 2016, the FASB issued Accounting Standards Update No. 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients. The amendments do not change the core revenue recognition principle in Topic 606. The amendments provide clarifying guidance in certain narrow areas and add some practical expedients. These amendments are effective at the same date that Topic 606 is effective. Topic 606 is effective for public entities for annual reporting periods beginning after December 15, 2017, including interim reporting periods therein (i.e., January 1, 2018, for a calendar year entity). Topic 606 is effective for nonpublic entities one year later. The Company is currently assessing the impact of the adoption of the amendment to Topic 606 and these amendments on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments”. The standard provides guidance on how certain cash receipts and payments are presented and classified in the statement of cash flows, including beneficial interests in securitization, which would impact the presentation of the deferred purchase price from sales of receivables. The standard is intended to reduce current diversity in practice. Early adoption is permitted, including adoption in an interim period. The Company does not expect the adoption of these amendments to have a significant impact on its consolidated financial statements.

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

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Our senior management is responsible for establishing and maintaining a system of disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, (the "Exchange Act") designed to ensure that the information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

When we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of December 31, 2015, our Chief Executive Officer and our Chief Accounting Officer concluded that as of such date, our disclosure controls and procedures were not effective due to a material weakness related to (i) the inability of our internal accounting personnel to identify, analyze, record and disclose the tax and financial reporting implications of certain complex accounting matters related to non-standard and unusual transactions and (ii) inventory accounting, in particular with respect to tracking for the aging of certain items reserving for slow moving inventory and obsolescence and, consequently, valuation of our inventory. In an effort to eliminate such weakness, we added Marianne Giglio to our accounting department and entered into an agreement with Chord Advisors, LLC, an advisory firm that provides financial accounting and advisory services to public companies, to assist our internal accounting staff in determining the appropriate tax and financial accounting treatment of our significant transactions and in connection with such other financial reporting matters as our management deems appropriate. More recently, effective October 3, 2016, Michael Recca became our Chief Financial Officer. Those actions have yet to have a significant impact on the effectiveness of our disclosure controls and procedures

We have evaluated the effectiveness of the design and operation of our disclosure controls and procedures under the supervision of and with the participation of management, including the Chief Executive Officer and our Chief Accounting Officer as of the end of the period covered by this Report. Based on that evaluation, our Chief Executive Officer and our Chief Accounting Officer have concluded that as of the end of the period covered by this report, our disclosure controls and procedures were not effective.

(b) Changes in Internal Control over Financial Reporting

There have not been any changes in our internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, during our most recently completed fiscal quarter which is the subject of this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II

OTHER INFORMATION

Item 1A. Risk Factors.

Reference is made to the risks and uncertainties disclosed in our 2015 Form 10-K and Q2 2016 Form 10-Q, which are incorporated by reference into this report. Prospective investors are encouraged to consider the risks described in our 2015 Form 10-K, Q2 2016 Form 10-Q, our Management's Discussion and Analysis of Financial Condition and Results of Operations contained in this Report and other information publicly disclosed or contained in documents we file with the Securities and Exchange Commission before purchasing our securities.

Item 6. Exhibits

<u>No.</u>	<u>Description</u>
4.1	Form of Warrant issued to purchasers of Notes in connection with Note Offering (incorporated herein by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on August 22, 2016).
4.2	Placement Agent Warrant issued to Taglich Brothers, Inc. in connection with Note Offering.
10.1	Thirteenth Amendment to PNC Loan Agreement (incorporated herein by reference to exhibit 10.4 to the Company's Current Report on Form 8-K filed on September 21, 2016).
10.2	Promissory note in the principal amount of \$500,000 payable to Michael Taglich (incorporated herein by reference to exhibit 10.1 to the Company's Current Report on Form 8-K filed on August 5, 2016).
10.3	Promissory note in the principal amount of \$1,000,000 payable to Michael Taglich (incorporated herein by reference to exhibit 3.1 to the Company's Current Report on Form 8-K filed on August 5, 2016).
10.4	Placement Agency Agreement dated August 19, 2016 between the Company and Taglich Brothers, Inc. (incorporated herein by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on August 22, 2016).
10.5	Securities Purchase Agreement by and among the Company and the purchasers named therein (incorporated herein by reference to Exhibit 10.2 to the Company's Current Report on Form 8-K filed on August 22, 2016).
10.6	The Company's 12% Convertible Subordinated Note due December 31, 2017(incorporated herein by reference to Exhibit 10.3 to the Company's Current Report on Form 8-K filed on August 22, 2016).
10.7	Joinder Agreement among the purchasers of the Notes and the Company (incorporated herein by reference to Exhibit 10.4 to the Company's Current Report on Form 8-K filed on August 22, 2016).
10.8	Amendment to Registration Rights Agreement (incorporated herein by reference to Exhibit 10.6 to the Company's Current Report on Form 8-K filed on August 22, 2016).
10.9	2016 Equity Incentive Plan.
31.1	Certification of the Principal Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of the Principal Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended.
32.1	Certification of the Principal Executive Officer pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of the Principal Financial Officer pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document*
101.SCH	XBRL Taxonomy Extension Schema*
101.CAL	XBRL Taxonomy Extension Calculation*
101.DEF	XBRL Taxonomy Extension Definition*
101.LAB	XBRL Taxonomy Extension Label*
101.PRE	XBRL Taxonomy Extension Presentation*

 * To be filed by Amendment

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 duly authorized.

Dated: November 14, 2016

AIR INDUSTRIES GROUP

By: /s/ Daniel R. Godin
Daniel R. Godin
President and CEO
(Principal Executive Officer)

By: /s/ Michael Recca
Michael Recca
Chief Financial Officer
(Principal Financial Officer)

NEITHER THIS SECURITY NOR THE SECURITIES FOR WHICH THIS SECURITY IS EXERCISABLE HAVE BEEN REGISTERED WITH THE SECURITIES AND EXCHANGE COMMISSION OR THE SECURITIES COMMISSION OF ANY STATE IN RELIANCE UPON AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), AND, ACCORDINGLY, MAY NOT BE OFFERED OR SOLD EXCEPT PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT OR PURSUANT TO AN AVAILABLE EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND IN ACCORDANCE WITH APPLICABLE STATE SECURITIES LAWS. THIS SECURITY AND THE SECURITIES ISSUABLE UPON EXERCISE OF THIS SECURITY MAY BE PLEDGED IN CONNECTION WITH A BONA FIDE MARGIN ACCOUNT OR OTHER LOAN SECURED BY SUCH SECURITIES.

COMMON STOCK PURCHASE WARRANT

AIR INDUSTRIES GROUP

Warrant Shares: 68,617

Initial Exercise Date: September 1, 2017

THIS COMMON STOCK PURCHASE WARRANT (the "Warrant") certifies that, for value received, Taglich Brothers, Inc. or its assigns (the "Holder") is entitled, upon the terms and subject to the limitations on exercise and the conditions hereinafter set forth, at any time on or after September 1, 2017 (the "Initial Exercise Date") and on or prior to the close of business on July 31, 2021 (the "Termination Date") but not thereafter, to subscribe for and purchase from Air Industries Group, a Nevada corporation (the "Company"), up to 68,617 shares (as subject to adjustment hereunder, the "Warrant Shares") of the Company's common stock ("Common Stock"). The purchase price of one share of Common Stock under this Warrant shall be equal to the Exercise Price, as defined in Section 2(b).

Section 1. Definitions. In addition to the terms defined elsewhere in this Agreement, the following terms have the meanings indicated in this Section 1:

"Affiliate" means any Person that, directly or indirectly through one or more intermediaries, controls or is controlled by or is under common control with a Person, as such terms are used in and construed under Rule 405 under the Securities Act.

"Board of Directors" means the board of directors of the Company.

"Business Day" means any day except any Saturday, any Sunday, any day which is a federal legal holiday in the United States or any day on which banking institutions in the State of New York are authorized or required by law or other governmental action to close.

“Commission” means the United States Securities and Exchange Commission.

“Exchange Act” means the Securities Exchange Act of 1934, as amended, and the rules and regulations promulgated thereunder.

“Liens” means a lien, charge pledge, security interest, encumbrance, right of first refusal, preemptive right or other restriction.

“Person” means an individual or corporation, partnership, trust, incorporated or unincorporated association, joint venture, limited liability company, joint stock company, government (or an agency or subdivision thereof) or other entity of any kind.

“Proceeding” means an action, claim, suit, investigation or proceeding (including, without limitation, an informal investigation or partial proceeding, such as a deposition), whether commenced or threatened.

“Rule 144” means Rule 144 promulgated by the Commission pursuant to the Securities Act, as such Rule may be amended or interpreted from time to time, or any similar rule or regulation hereafter adopted by the Commission having substantially the same purpose and effect as such Rule.

“Securities Act” means the Securities Act of 1933, as amended, and the rules and regulations promulgated thereunder.

“Trading Day” means a day on which the Common Stock is traded on a Trading Market.

“Trading Market” means any of the following markets or exchanges on which the Common Stock is listed or quoted for trading on the date in question: the NYSE MKT, the Nasdaq Capital Market, the Nasdaq Global Market, the Nasdaq Global Select Market, the New York Stock Exchange or the OTCQB or OTCQX (or any successors to any of the foregoing).

“Transfer Agent” means Broadridge Corporate Issuer Solutions, Inc., the current transfer agent of the Company, with a mailing address of PO Box 1342, Brentwood, New York 11717 and a facsimile number of (215) 553-5402, and any successor transfer agent of the Company.

“VWAP” means, for any date, the price determined by the first of the following clauses that applies: (a) if the Common Stock is then listed or quoted on a Trading Market, the daily volume weighted average price of the Common Stock for such date (or the nearest preceding date) on the Trading Market on which the Common Stock is then listed or quoted as reported by Bloomberg L.P. (based on a Trading Day from 9:30 a.m. (New York City time) to 4:02 p.m. (New York City time)), (b) if the OTCQB or OTCQX is not a Trading Market, the volume weighted average price of the Common Stock for such date (or the nearest preceding date) on the OTCQB or OTCQX, (c) if the Common Stock is not then listed or quoted for trading on the OTCQB or OTCQX and if prices for the Common Stock are then reported in the “Pink Sheets” published by Pink OTC Markets Group, Inc. (or a similar organization or agency succeeding to its functions of reporting prices), the most recent bid price per share of the Common Stock so reported, or (d) in all other cases, the fair market value of a share of Common Stock as determined by an independent appraiser selected in good faith by the Holder and reasonably acceptable to the Company, the fees and expenses of which shall be paid by the Company.

Section 2. Exercise.

a) Exercise of Warrant. Exercise of the purchase rights represented by this Warrant may be made, in whole or in part, at any time or times on or after the Initial Exercise Date and on or before the Termination Date by delivery to the Company (or such other office or agency of the Company as it may designate by notice in writing to the registered Holder at the address of the Holder appearing on the books of the Company) of a duly executed facsimile copy (or e-mail attachment) of the Notice of Exercise form annexed hereto. Within three (3) Trading Days following the date of exercise as aforesaid, the Holder shall deliver the aggregate Exercise Price for the shares specified in the applicable Notice of Exercise by wire transfer or cashier's check drawn on a United States bank unless the cashless exercise procedure specified in Section 2(c) below is specified in the applicable Notice of Exercise. No ink-original Notice of Exercise shall be required, nor shall any medallion guarantee (or other type of guarantee or notarization) of any Notice of Exercise form be required. Notwithstanding anything herein to the contrary, the Holder shall not be required to physically surrender this Warrant to the Company until the Holder has purchased all of the Warrant Shares available hereunder and the Warrant has been exercised in full, in which case, the Holder shall surrender this Warrant to the Company for cancellation within three (3) Trading Days of the date the final Notice of Exercise is delivered to the Company. Partial exercises of this Warrant resulting in purchases of a portion of the total number of Warrant Shares available hereunder shall have the effect of lowering the outstanding number of Warrant Shares purchasable hereunder in an amount equal to the applicable number of Warrant Shares purchased. The Holder and the Company shall maintain records showing the number of Warrant Shares purchased and the date of such purchases. The Company shall deliver any objection to any Notice of Exercise within one (1) Business Day of receipt of such notice. **The Holder and any assignee, by acceptance of this Warrant, acknowledge and agree that, by reason of the provisions of this paragraph, following the purchase of a portion of the Warrant Shares hereunder, the number of Warrant Shares available for purchase hereunder at any given time may be less than the amount stated on the face hereof.**

b) Exercise Price. The exercise price per share of the Common Stock under this Warrant shall be \$6.15, subject to adjustment hereunder (the "Exercise Price").

c) Cashless Exercise. If at the time of exercise hereof there is no effective registration statement registering for sale or resale the Warrant Shares, then this Warrant may also be exercised, in whole or in part, at such time by means of a "cashless exercise" in which the Holder shall be entitled to receive a number of Warrant Shares equal to the quotient obtained by dividing [(A-B) (X)] by (A), where:

(A) = the last VWAP immediately preceding the time of delivery of the Notice of Exercise giving rise to the applicable “cashless exercise”, as set forth in the applicable Notice of Exercise (to clarify, the “last VWAP” will be the last VWAP as calculated over an entire Trading Day such that, in the event that this Warrant is exercised at a time that the Trading Market is open, the prior Trading Day’s VWAP shall be used in this calculation);

(B) = the Exercise Price of this Warrant, as adjusted hereunder; and

(X) = the number of Warrant Shares that would be issuable upon exercise of this Warrant in accordance with the terms of this Warrant if such exercise were by means of a cash exercise rather than a cashless exercise.

If Warrant Shares are issued in such a cashless exercise, the parties acknowledge and agree that in accordance with Section 3(a)(9) of the Securities Act, the Warrant Shares shall take on the registered characteristics of the Warrants being exercised, and the holding period of the Warrants being exercised may be tacked on to the holding period of the Warrant Shares. The Company agrees not to take any position contrary to this Section 2(c).

d) Mechanics of Exercise.

i. Delivery of Warrant Shares Upon Exercise. The Company shall cause the Warrant Shares purchased hereunder to be transmitted by the Transfer Agent to the Holder by crediting the account of the Holder’s or its designee’s balance account with The Depository Trust Company through its Deposit or Withdrawal at Custodian system (“DWAC”) if the Company is then a participant in such system and either (A) there is an effective registration statement permitting the issuance of the Warrant Shares to or resale of the Warrant Shares by Holder or (B) this Warrant is being exercised via cashless exercise, and otherwise by physical delivery of a certificate, registered in the Company’s share register in the name of the holder or its designee, for the number of Warrant Shares to which the Holder is entitled pursuant to such exercise to the address specified by the Holder in the Notice of Exercise by the date that is three (3) Trading Days after the delivery to the Company of the Notice of Exercise (such date, the “Warrant Share Delivery Date”). Upon delivery of the Notice of Exercise the Holder shall be deemed for all corporate purposes to have become the holder of record of the Warrant Shares with respect to which this Warrant has been exercised, irrespective of the date of delivery of the Warrant Shares; provided payment of the aggregate Exercise Price (other than in the case of a Cashless Exercise) is received within three Trading Days of delivery of the Notice of Exercise. The Company agrees to maintain a transfer agent that is a participant in the FAST program so long as this warrant remains outstanding and exercisable.

ii. Delivery of New Warrants Upon Exercise. If this Warrant shall have been exercised in part, the Company shall, at the request of a Holder and upon surrender of this Warrant certificate, at the time of delivery of the Warrant Shares, deliver to the Holder a new Warrant evidencing the rights of the Holder to purchase the unpurchased Warrant Shares called for by this Warrant, which new Warrant shall in all other respects be identical with this Warrant.

iii. Rescission Rights. If the Company fails to cause the Transfer Agent to transmit to the Holder the Warrant Shares pursuant to Section 2(d)(i) by the Warrant Share Delivery Date, then the Holder will have the right to rescind such exercise.

iv. Compensation for Buy-In on Failure to Timely Deliver Warrant Shares Upon Exercise. In addition to any other rights available to the Holder, if the Company fails to cause the Transfer Agent to transmit to the Holder the Warrant Shares in accordance with the provisions of Section 2(d)(i) above pursuant to an exercise on or before the Warrant Share Delivery Date, and if after such date the Holder is required by its broker to purchase (in an open market transaction or otherwise) or the Holder's brokerage firm otherwise purchases, shares of Common Stock to deliver in satisfaction of a sale by the Holder of the Warrant Shares which the Holder anticipated receiving upon such exercise (a "Buy-In"), then the Company shall (A) pay in cash to the Holder the amount, if any, by which (x) the Holder's total purchase price (including brokerage commissions, if any) for the shares of Common Stock so purchased exceeds (y) the amount obtained by multiplying (1) the number of Warrant Shares that the Company was required to deliver to the Holder in connection with the exercise at issue times (2) the price at which the sell order giving rise to such purchase obligation was executed, and (B) at the option of the Holder, either reinstate the portion of the Warrant and equivalent number of Warrant Shares for which such exercise was not honored (in which case such exercise shall be deemed rescinded) or deliver to the Holder the number of shares of Common Stock that would have been issued had the Company timely complied with its exercise and delivery obligations hereunder. For example, if the Holder purchases Common Stock having a total purchase price of \$11,000 to cover a Buy-In with respect to an attempted exercise of shares of Common Stock with an aggregate sale price giving rise to such purchase obligation of \$10,000, under clause (A) of the immediately preceding sentence the Company shall be required to pay the Holder \$1,000. The Holder shall provide the Company written notice indicating the amounts payable to the Holder in respect of the Buy-In and, upon request of the Company, evidence of the amount of such loss. Nothing herein shall limit a Holder's right to pursue any other remedies available to it hereunder, at law or in equity including, without limitation, a decree of specific performance and/or injunctive relief with respect to the Company's failure to timely deliver shares of Common Stock upon exercise of the Warrant as required pursuant to the terms hereof.

v. No Fractional Shares or Scrip. No fractional shares or scrip representing fractional shares shall be issued upon the exercise of this Warrant. As to any fraction of a share which the Holder would otherwise be entitled to purchase upon such exercise, the Company shall, at its election, either pay a cash adjustment in respect of such final fraction in an amount equal to such fraction multiplied by the Exercise Price or round up to the next whole share.

vi. Charges, Taxes and Expenses. Issuance of Warrant Shares shall be made without charge to the Holder for any issue or transfer tax or other incidental expense in respect of the issuance of such Warrant Shares, all of which taxes and expenses shall be paid by the Company, and such Warrant Shares shall be issued in the name of the Holder or in such name or names as may be directed by the Holder; provided, however, that in the event Warrant Shares are to be issued in a name other than the name of the Holder, this Warrant when surrendered for exercise shall be accompanied by the Assignment Form attached hereto duly executed by the Holder and the Company may require, as a condition thereto, the payment of a sum sufficient to reimburse it for any transfer tax incidental thereto. The Company shall pay all Transfer Agent fees required for same-day processing of any Notice of Exercise and all fees to the Depository Trust Company (or another established clearing corporation performing similar functions) required for same-day electronic delivery of the Warrant Shares.

vii. Closing of Books. The Company will not close its stockholder books or records in any manner which prevents the timely exercise of this Warrant, pursuant to the terms hereof.

Section 3. Certain Adjustments.

a) Stock Dividends and Splits. If the Company, at any time while this Warrant is outstanding: (i) pays a stock dividend or otherwise makes a distribution or distributions on shares of its Common Stock or any other equity or equity equivalent securities payable in shares of Common Stock (which, for avoidance of doubt, shall not include any shares of Common Stock issued by the Company upon exercise of this Warrant), (ii) subdivides outstanding shares of Common Stock into a larger number of shares, (iii) combines (including by way of reverse stock split) outstanding shares of Common Stock into a smaller number of shares or (iv) issues by reclassification of shares of the Common Stock any shares of capital stock of the Company, then in each case the Exercise Price shall be multiplied by a fraction of which the numerator shall be the number of shares of Common Stock (excluding treasury shares, if any) outstanding immediately before such event and of which the denominator shall be the number of shares of Common Stock outstanding immediately after such event, and the number of shares issuable upon exercise of this Warrant shall be proportionately adjusted such that the aggregate Exercise Price of this Warrant shall remain unchanged. Any adjustment made pursuant to this Section 3(a) shall become effective immediately after the record date for the determination of stockholders entitled to receive such dividend or distribution and shall become effective immediately after the effective date in the case of a subdivision, combination or re-classification.

b) Subsequent Rights Offerings. In addition to any adjustments pursuant to Section 3(a) above, if at any time the Company grants, issues or sells any Common Stock Equivalents or rights to purchase stock, warrants, securities or other property pro rata to the record holders of any class of shares of Common Stock (the "Purchase Rights"), then the Holder will be entitled to acquire, upon the terms applicable to such Purchase Rights, the aggregate Purchase Rights which the Holder could have acquired if the Holder had held the number of shares of Common Stock acquirable upon complete exercise of this Warrant immediately before the date on which a record is taken for the grant, issuance or sale of such Purchase Rights, or, if no such record is taken, the date as of which the record holders of shares of Common Stock are to be determined for the grant, issue or sale of such Purchase Rights.

c) Pro Rata Distributions. During such time as this Warrant is outstanding, if the Company shall declare or make any dividend or other distribution of its assets (or rights to acquire its assets) to holders of shares of Common Stock, by way of return of capital or otherwise (including, without limitation, any distribution of cash, stock or other securities, property or options by way of a dividend, spin off, reclassification, corporate rearrangement, scheme of arrangement or other similar transaction) (a "Distribution"), at any time after the issuance of this Warrant, then, in each such case, the Holder shall be entitled to participate in such Distribution to the same extent that the Holder would have participated therein if the Holder had held the number of shares of Common Stock acquirable upon complete exercise of this Warrant immediately before the date of which a record is taken for such Distribution, or, if no such record is taken, the date as of which the record holders of shares of Common Stock are to be determined for the participation in such Distribution.

d) Fundamental Transaction. If, at any time while this Warrant is outstanding, (i) the Company, directly or indirectly, in one or more related transactions effects any merger or consolidation of the Company with or into another Person, (ii) the Company, directly or indirectly, effects any sale, lease, license, assignment, transfer, conveyance or other disposition of all or substantially all of its assets in one or a series of related transactions, (iii) any, direct or indirect, purchase offer, tender offer or exchange offer (whether by the Company or another Person) is completed pursuant to which holders of Common Stock are permitted to sell, tender or exchange their shares for other securities, cash or property and has been accepted by the holders of 50% or more of the outstanding Common Stock, (iv) the Company, directly or indirectly, in one or more related transactions effects any reclassification, reorganization or recapitalization of the Common Stock or any compulsory share exchange pursuant to which the Common Stock is effectively converted into or exchanged for other securities, cash or property, or (v) the Company, directly or indirectly, in one or more related transactions consummates a stock or share purchase agreement or other business combination (including, without limitation, a reorganization, recapitalization, spin-off or scheme of arrangement) with another Person or group of Persons whereby such other Person or group acquires more than 50% of the outstanding shares of Common Stock (not including any shares of Common Stock held by the other Person or other Persons making or party to, or associated or affiliated with the other Persons making or party to, such stock or share purchase agreement or other business combination) (each a "Fundamental Transaction"), then, upon any subsequent exercise of this Warrant, the Holder shall have the right to receive, for each Warrant Share that would have been issuable upon such exercise immediately prior to the occurrence of such Fundamental Transaction, at the option of the Holder (without regard to any limitation in Section 2(e) on the exercise of this Warrant), the number of shares of Common Stock of the successor or acquiring corporation or of the Company, if it is the surviving corporation, and any additional consideration (the "Alternate Consideration") receivable as a result of such Fundamental Transaction by a holder of the number of shares of Common Stock for which this Warrant is exercisable immediately prior to such Fundamental Transaction (without regard to any limitation in Section 2(e) on the exercise of this Warrant). For purposes of any such exercise, the determination of the Exercise Price shall be appropriately adjusted to apply to such Alternate Consideration based on the amount of Alternate Consideration issuable in respect of one share of Common Stock in such Fundamental Transaction, and the Company shall apportion the Exercise Price among the Alternate Consideration in a reasonable manner reflecting the

relative value of any different components of the Alternate Consideration. If holders of Common Stock are given any choice as to the securities, cash or property to be received in a Fundamental Transaction, then the Holder shall be given the same choice as to the Alternate Consideration it receives upon any exercise of this Warrant following such Fundamental Transaction. The Company shall cause any successor entity in a Fundamental Transaction in which the Company is not the survivor (the “Successor Entity”) to assume in writing all of the obligations of the Company under this Warrant and the other Transaction Documents in accordance with the provisions of this Section 3(e) pursuant to written agreements in form and substance reasonably satisfactory to the Holder and approved by the Holder (without unreasonable delay) prior to such Fundamental Transaction and shall, at the option of the Holder, deliver to the Holder in exchange for this Warrant a security of the Successor Entity evidenced by a written instrument substantially similar in form and substance to this Warrant which is exercisable for a corresponding number of shares of capital stock of such Successor Entity (or its parent entity) equivalent to the shares of Common Stock acquirable and receivable upon exercise of this Warrant (without regard to any limitations on the exercise of this Warrant) prior to such Fundamental Transaction, and with an exercise price which applies the exercise price hereunder to such shares of capital stock (but taking into account the relative value of the shares of Common Stock pursuant to such Fundamental Transaction and the value of such shares of capital stock, such number of shares of capital stock and such exercise price being for the purpose of protecting the economic value of this Warrant immediately prior to the consummation of such Fundamental Transaction), and which is reasonably satisfactory in form and substance to the Holder. Upon the occurrence of any such Fundamental Transaction, the Successor Entity shall succeed to, and be substituted for (so that from and after the date of such Fundamental Transaction, the provisions of this Warrant and the other Transaction Documents referring to the “Company” shall refer instead to the Successor Entity), and may exercise every right and power of the Company and shall assume all of the obligations of the Company under this Warrant and the other Transaction Documents with the same effect as if such Successor Entity had been named as the Company herein.

e) Calculations. All calculations under this Section 3 shall be made to the nearest cent or the nearest 1/100th of a share, as the case may be. For purposes of this Section 3, the number of shares of Common Stock deemed to be issued and outstanding as of a given date shall be the sum of the number of shares of Common Stock (excluding treasury shares, if any) issued and outstanding.

f) Notice to Holder.

i. Adjustment to Exercise Price. Whenever the Exercise Price is adjusted pursuant to any provision of this Section 3, the Company shall promptly deliver to the Holder by facsimile or email a notice setting forth the Exercise Price after such adjustment and any resulting adjustment to the number of Warrant Shares and setting forth a brief statement of the facts requiring such adjustment.

ii. Notice to Allow Exercise by Holder. If (A) the Company shall declare a dividend (or any other distribution in whatever form) on the Common Stock, (B) the Company shall declare a special nonrecurring cash dividend on or a redemption of the Common Stock, (C) the Company shall authorize the granting to all holders of the Common Stock rights or warrants to subscribe for or purchase any shares of capital stock of any class or of any rights, (D) the approval of any stockholders of the Company shall be required in connection with any reclassification of the Common Stock, any consolidation or merger to which the Company is a party, any sale or transfer of all or substantially all of the assets of the Company, or any compulsory share exchange whereby the Common Stock is converted into other securities, cash or property, or (E) the Company shall authorize the voluntary or involuntary dissolution, liquidation or winding up of the affairs of the Company, then, in each case, the Company shall cause to be delivered by facsimile or email to the Holder at its last facsimile number or email address as it shall appear upon the Warrant Register of the Company, at least 20 calendar days prior to the applicable record or effective date hereinafter specified, a notice stating (x) the date on which a record is to be taken for the purpose of such dividend, distribution, redemption, rights or warrants, or if a record is not to be taken, the date as of which the holders of the Common Stock of record to be entitled to such dividend, distributions, redemption, rights or warrants are to be determined or (y) the date on which such reclassification, consolidation, merger, sale, transfer or share exchange is expected to become effective or close, and the date as of which it is expected that holders of the Common Stock of record shall be entitled to exchange their shares of the Common Stock for securities, cash or other property deliverable upon such reclassification, consolidation, merger, sale, transfer or share exchange; provided that the failure to deliver such notice or any defect therein or in the delivery thereof shall not affect the validity of the corporate action required to be specified in such notice. The Holder shall remain entitled to exercise this Warrant during the period commencing on the date of such notice to the effective date of the event triggering such notice except as may otherwise be expressly set forth herein.

Section 4. Transfer of Warrant.

a) Transferability. Subject to compliance with any applicable securities laws and the conditions set forth in Section 4(d) hereof, this Warrant and all rights hereunder (including, without limitation, any registration rights) are transferable, in whole or in part, upon surrender of this Warrant at the principal office of the Company or its designated agent, together with a written assignment of this Warrant substantially in the form attached hereto duly executed by the Holder or its agent or attorney and funds sufficient to pay any transfer taxes payable upon the making of such transfer. Upon such surrender and, if required, such payment, the Company shall execute and deliver a new Warrant or Warrants in the name of the assignee or assignees, as applicable, and in the denomination or denominations specified in such instrument of assignment, and shall issue to the assignor a new Warrant evidencing the portion of this Warrant not so assigned, and this Warrant shall promptly be cancelled. The Warrant, if properly assigned in accordance herewith, may be exercised by a new holder for the purchase of Warrant Shares without having a new Warrant issued.

b) New Warrants. This Warrant may be divided or combined with other Warrants upon presentation hereof at the aforesaid office of the Company, together with a written notice specifying the names and denominations in which new Warrants are to be issued, signed by the Holder or its agent or attorney. Subject to compliance with Section 4(a), as to any transfer which may be involved in such division or combination, the Company shall execute and deliver a new Warrant or Warrants in exchange for the Warrant or Warrants to be divided or combined in accordance with such notice. All Warrants issued on transfers or exchanges shall be dated the Initial Exercise Date and shall be identical with this Warrant except as to the number of Warrant Shares issuable pursuant thereto.

c) Warrant Register. The Company shall register this Warrant, upon records to be maintained by the Company for that purpose (the "Warrant Register"), in the name of the record Holder hereof from time to time. The Company may deem and treat the registered Holder of this Warrant as the absolute owner hereof for the purpose of any exercise hereof or any distribution to the Holder, and for all other purposes, absent actual notice to the contrary.

d) Transfer Restrictions. (i) If, at the time of the surrender of this Warrant in connection with any transfer of this Warrant, the transfer of this Warrant shall not be either (i) registered pursuant to an effective registration statement under the Securities Act and under applicable state securities or blue sky laws or (ii) eligible for resale without volume or manner-of-sale restrictions or current public information requirements pursuant to Rule 144, the Company may require, as a condition of allowing such transfer, that the Holder or transferee of this Warrant, as the case may be, provides to the Company an opinion of counsel, the form and substance of which opinion shall be reasonably satisfactory to the Company, to the effect that the transfer of this Warrant does not require registration under the Securities Act.

(ii) Neither this Warrant nor the Warrant Shares and any other securities issuable upon exercise hereof, may be transferred whether by sale assignment, gift or otherwise, by the Holder prior to March 1, 2017 (such period, the "Restriction Period"), except for transfers to employees of the original Holder who will be subject to the provisions of this subsection. The Holder will not offer, sell, contract to sell, hypothecate, pledge or otherwise dispose of (or enter into any transaction which is designed to, or might reasonably be expected to, result in the disposition (whether by actual disposition or effective economic disposition due to cash settlement or otherwise) by the Holder of this Warrant, the Warrant Shares and any other securities issuable upon exercise hereof.

e) Representation by the Holder. The Holder, by the acceptance hereof, represents and warrants that it is acquiring this Warrant and, upon any exercise hereof, will acquire the Warrant Shares issuable upon such exercise, for its own account and not with a view to or for distributing or reselling such Warrant Shares or any part thereof in violation of the Securities Act or any applicable state securities law, except pursuant to sales registered or exempted under the Securities Act.

Section 5. Miscellaneous.

a) No Rights as Stockholder Until Exercise. This Warrant does not entitle the Holder to any voting rights, dividends or other rights as a stockholder of the Company prior to the exercise hereof as set forth in Section 2(d)(i), except as expressly set forth in Section 3.

b) Loss, Theft, Destruction or Mutilation of Warrant. The Company covenants that upon receipt by the Company of evidence reasonably satisfactory to it of the loss, theft, destruction or mutilation of this Warrant or any stock certificate relating to the Warrant Shares, and in case of loss, theft or destruction, of indemnity or security reasonably satisfactory to it (which, in the case of the Warrant, shall not include the posting of any bond), and upon surrender and cancellation of such Warrant or stock certificate, if mutilated, the Company will make and deliver a new Warrant or stock certificate of like tenor and dated as of such cancellation, in lieu of such Warrant or stock certificate.

c) Saturdays, Sundays, Holidays, etc. If the last or appointed day for the taking of any action or the expiration of any right required or granted herein shall not be a Business Day, then, such action may be taken or such right may be exercised on the next succeeding Business Day.

d) Authorized Shares. The Company covenants that, during the period the Warrant is outstanding, it will reserve from its authorized and unissued Common Stock a sufficient number of shares to provide for the issuance of the Warrant Shares upon the exercise of any purchase rights under this Warrant. The Company further covenants that its issuance of this Warrant shall constitute full authority to its officers who are charged with the duty of executing stock certificates to execute and issue the necessary Warrant Shares upon the exercise of the purchase rights under this Warrant. The Company will take all such reasonable action as may be necessary to assure that such Warrant Shares may be issued as provided herein without violation of any applicable law or regulation, or of any requirements of the Trading Market upon which the Common Stock may be listed. The Company covenants that all Warrant Shares which may be issued upon the exercise of the purchase rights represented by this Warrant will, upon exercise of the purchase rights represented by this Warrant and payment for such Warrant Shares in accordance herewith, be duly authorized, validly issued, fully paid and nonassessable and free from all taxes, liens and charges created by the Company in respect of the issue thereof (other than taxes in respect of any transfer occurring contemporaneously with such issue).

Except and to the extent as waived or consented to by the Holder, the Company shall not by any action, including, without limitation, amending its certificate of incorporation or through any reorganization, transfer of assets, consolidation, merger, dissolution, issue or sale of securities or any other voluntary action, avoid or seek to avoid the observance or performance of any of the terms of this Warrant, but will at all times in good faith assist in the carrying out of all such terms and in the taking of all such actions as may be necessary or appropriate to protect the rights of Holder as set forth in this Warrant against impairment. Without limiting the generality of the foregoing, the Company will (i) not increase the par value of any Warrant Shares above the amount payable therefor upon such exercise immediately prior to such increase in par value, (ii) take all such action as may be necessary or appropriate in order that the Company may validly and legally issue fully paid and nonassessable Warrant Shares upon the exercise of this Warrant and (iii) use commercially reasonable efforts to obtain all such authorizations, exemptions or consents from any public regulatory body having jurisdiction thereof, as may be, necessary to enable the Company to perform its obligations under this Warrant.

Before taking any action which would result in an adjustment in the number of Warrant Shares for which this Warrant is exercisable or in the Exercise Price, the Company shall obtain all such authorizations or exemptions thereof, or consents thereto, as may be necessary from any public regulatory body or bodies having jurisdiction thereof.

e) Governing Law. All questions concerning the construction, validity, enforcement and interpretation of this Warrant shall be governed by and construed and enforced in accordance with the internal laws of the State of New York, without regard to the principles of conflict of laws thereof. Each party agrees that all legal proceedings concerning the interpretation, enforcement and defense of this Warrant shall be commenced in the state and federal courts sitting in the City of New York, Borough of Manhattan (the "New York Courts"). Each party hereto hereby irrevocably submits to the exclusive jurisdiction of the New York Courts for the adjudication of any dispute hereunder or in connection herewith or with any transaction contemplated hereby or discussed herein (including with respect to the enforcement of any of the Transaction Documents), and hereby irrevocably waives, and agrees not to assert in any suit, action or proceeding, any claim that it is not personally subject to the jurisdiction of such New York Courts, or such New York Courts are improper or inconvenient venue for such proceeding. Each party hereto hereby irrevocably waives, to the fullest extent permitted by applicable law, any and all right to trial by jury in any legal proceeding arising out of or relating to this Warrant. If any party shall commence an action or proceeding to enforce any provisions of this Warrant, then the prevailing party in such action or proceeding shall be reimbursed by the other party for its attorneys' fees and other costs and expenses incurred in the investigation, preparation and prosecution of such action or proceeding.

f) Restrictions. The Holder acknowledges that the Warrant Shares acquired upon the exercise of this Warrant, if not registered and the Holder does not utilize cashless exercise, will have restrictions upon resale imposed by state and federal securities laws.

g) Nonwaiver and Expenses. No course of dealing or any delay or failure to exercise any right hereunder on the part of Holder shall operate as a waiver of such right or otherwise prejudice the Holder's rights, powers or remedies, notwithstanding the fact that all rights hereunder terminate on the Termination Date. If the Company willfully and knowingly fails to comply with any provision of this Warrant, which results in any material damages to the Holder, the Company shall pay to the Holder such amounts as shall be sufficient to cover any costs and expenses including, but not limited to, reasonable attorneys' fees, including those of appellate proceedings, incurred by the Holder in collecting any amounts due pursuant hereto or in otherwise enforcing any of its rights, powers or remedies hereunder.

h) Notices. Any and all notices or other communications or deliveries to be provided by the Holders hereunder including, without limitation, any Notice of Exercise, shall be in writing and delivered personally, by facsimile, or sent by a nationally recognized overnight courier service, addressed to the Company, at the address set forth above **Attention:** Daniel R. Godin, facsimile number (631) 206-9152, email address mrecca@airindustriestgroup.com, with a copy to Daniel R. Godin at Dgodin@airindustriestgroup.com or such other facsimile number, email address or address as the Company may specify for such purposes by notice to the Holders. Any and all notices or other communications or deliveries to be provided by the Company hereunder shall be in writing and delivered personally, by facsimile, or sent by a nationally recognized overnight courier service addressed to each Holder at the facsimile number or address of such Holder appearing on the books of the Company, or if no such facsimile number or address appears on the books of the Company. Any notice or other communication or deliveries hereunder shall be deemed given and effective on the earliest of (i) the date of transmission, if such notice or communication is delivered via facsimile at the facsimile number set forth in this Section prior to 5:30 p.m. (New York City time) on any date, (ii) the next Trading Day after the date of transmission, if such notice or communication is delivered via facsimile at the facsimile number set forth in this Section on a day that is not a Trading Day or later than 5:30 p.m. (New York City time) on any Trading Day, (iii) the second Trading Day following the date of mailing, if sent by U.S. nationally recognized overnight courier service, or (iv) upon actual receipt by the party to whom such notice is required to be given.

i) Limitation of Liability. No provision hereof, in the absence of any affirmative action by the Holder to exercise this Warrant to purchase Warrant Shares, and no enumeration herein of the rights or privileges of the Holder, shall give rise to any liability of the Holder for the purchase price of any Common Stock or as a stockholder of the Company, whether such liability is asserted by the Company or by creditors of the Company.

j) Remedies. The Holder, in addition to being entitled to exercise all rights granted by law, including recovery of damages, will be entitled to specific performance of its rights under this Warrant. The Company agrees that monetary damages would not be adequate compensation for any loss incurred by reason of a breach by it of the provisions of this Warrant and hereby agrees to waive and not to assert the defense in any action for specific performance that a remedy at law would be adequate.

k) Successors and Assigns. Subject to applicable securities laws, this Warrant and the rights and obligations evidenced hereby shall inure to the benefit of and be binding upon the successors and permitted assigns of the Company and the successors and permitted assigns of Holder. The provisions of this Warrant are intended to be for the benefit of any Holder from time to time of this Warrant and shall be enforceable by the Holder or holder of Warrant Shares.

l) Amendment. This Warrant may be modified or amended or the provisions hereof waived with the written consent of the Company and the Holder.

m) Severability. Wherever possible, each provision of this Warrant shall be interpreted in such manner as to be effective and valid under applicable law, but if any provision of this Warrant shall be prohibited by or invalid under applicable law, such provision shall be ineffective to the extent of such prohibition or invalidity, without invalidating the remainder of such provisions or the remaining provisions of this Warrant.

n) Headings. The headings used in this Warrant are for the convenience of reference only and shall not, for any purpose, be deemed a part of this Warrant.

(Signature Page Follows)

IN WITNESS WHEREOF, the Company has caused this Warrant to be executed by its officer thereunto duly authorized as of the date first above indicated.

AIR INDUSTRIES GROUP

By: /s/ Daniel R. Godin
Daniel R. Godin
President and CEO

NOTICE OF EXERCISE

TO: AIR INDUSTRIES GROUP

(1) The undersigned hereby elects to purchase _____ Warrant Shares of the Company pursuant to the terms of the attached Warrant (only if exercised in full), and tenders herewith payment of the exercise price in full, together with all applicable transfer taxes, if any.

(2) Payment shall take the form of (check applicable box):

in lawful money of the United States; or

[if permitted] the cancellation of such number of Warrant Shares as is necessary, in accordance with the formula set forth in subsection 2(c), to exercise this Warrant with respect to the maximum number of Warrant Shares purchasable pursuant to the cashless exercise procedure set forth in subsection 2(c).

(3) Please issue said Warrant Shares in the name of the undersigned or in such other name as is specified below:

The Warrant Shares shall be delivered to the following DWAC Account Number:

[SIGNATURE OF HOLDER]

Name of Investing Entity: _____

Signature of Authorized Signatory of Investing Entity: _____

Name of Authorized Signatory: _____

Title of Authorized Signatory: _____

Date: _____

ASSIGNMENT FORM

(To assign the foregoing warrant, execute this form and supply required information. Do not use this form to exercise the warrant.)

FOR VALUE RECEIVED, _____ shares of Common Stock underlying the foregoing Warrant and all rights evidenced thereby are hereby assigned to _____.

Dated:

Holder's Signature:

Holder's Address:

NOTE: The signature to this Assignment Form must correspond with the name as it appears on the face of the Warrant, without alteration or enlargement or any change whatsoever. Officers of corporations and those acting in a fiduciary or other representative capacity should file proper evidence of authority to assign the foregoing Warrant.

AIR INDUSTRIES GROUP
2016 EQUITY INCENTIVE PLAN

1. Purposes of the Plan.

The purposes of this Equity Incentive Plan are to attract and retain the best available personnel, to provide additional incentive to Employees, Directors and Consultants and to promote the success of the Company's business.

2. Definitions.

As used herein, the following definitions shall apply:

(a) "Administrator" means the Board or any Committee appointed to administer the Plan.

(b) "Affiliate" and "Associate" shall have the respective meanings ascribed to such terms in Rule 12b-2 promulgated under the Exchange Act.

(c) "Applicable Laws" means the legal requirements relating to the administration of stock incentive plans, if any, under applicable provisions of federal securities laws, state corporate and securities laws, the Code, the rules of any applicable stock exchange or national market system, and the rules of any foreign jurisdiction applicable to Awards granted to residents therein.

(d) "Award" means the grant of an Option, SAR, Dividend Equivalent Right, Restricted Stock, Performance Unit, Performance Share, or other right or benefit under the Plan.

(e) "Award Agreement" means the written agreement evidencing the grant of an Award executed by the Company and the Grantee, including any amendments thereto.

(f) "Board" means the Board of Directors of the Company.

(g) "Cause" means, with respect to the termination by the Company or a Related Entity of the Grantee's Continuous Service, that such termination is for "Cause" as such term is expressly defined in a then-effective written agreement between the Grantee and the Company or such Related Entity, or in the absence of such then-effective written agreement and definition, is based on, in the determination of the Administrator, the Grantee's:

(i) refusal or failure to act in accordance with any specific, lawful direction or order of the Company or a Related Entity;

(ii) unfitness or unavailability for service or unsatisfactory performance (other than as a result of Disability);

(iii) performance of any act or failure to perform any act, in bad faith and to the detriment of the Company or a Related Entity;

(iv) dishonesty, intentional misconduct or material breach of any agreement with the Company or a Related Entity; or

(v) commission of a crime involving dishonesty, breach of trust, or physical or emotional harm to any person.

(h) "Code" means the Internal Revenue Code of 1986, as amended.

(i) "Committee" means any committee appointed by the Board to administer the Plan.

(j) "Common Stock" means the common stock of the Company.

(k) "Company" means Air Industries Group, a Nevada corporation.

(l) "Consultant" means any person (other than an Employee or a Director, solely with respect to rendering services in such person's capacity as a Director) who is engaged by the Company or any Related Entity to render consulting or advisory services to the Company or such Related Entity.

(m) "Continuous Service" means that the provision of services to the Company or a Related Entity in any capacity of Employee, Director or Consultant, is not interrupted or terminated. Continuous Service shall not be considered interrupted in the case of (i) any leave of absence approved by the Company or Related Entity, (ii) transfers between locations of the Company or among the Company, any Related Entity, or any successor, in any capacity of Employee, Director or Consultant, or (iii) any change in status as long as the individual remains in the service of the Company or a Related Entity in any capacity of Employee, Director or Consultant (except as otherwise provided in the Award Agreement). For purposes of Incentive Stock Options, no such approved leave of absence may exceed ninety (90) days, unless re-employment upon expiration of such leave is guaranteed by statute or contract.

(n) "Corporate Transaction" means any of the following transactions:

(i) a merger or consolidation in which the Company is not the surviving entity, except for a transaction the principal purpose of which is to change the state in which the Company is incorporated;

(ii) the sale, transfer or other disposition of all or substantially all of the assets of the Company (including the capital stock of the Company's subsidiary corporations) in connection with the complete liquidation or dissolution of the Company;

(iii) any reverse merger in which the Company is the surviving entity but in which securities possessing more than eighty percent (80%) of the total combined voting power of the Company's outstanding securities are transferred to a person or persons different from those who held such securities immediately prior to such merger; or

(iv) an acquisition by any person or related group of persons (other than the Company or by a Company-sponsored employee benefit plan) of beneficial ownership (within the meaning of Rule 13d-3 of the Exchange Act) of securities possessing more than eighty percent (80%) of the total combined voting power of the Company's outstanding securities, but excluding any such transaction that the Administrator determines shall not be a Corporate Transaction.

(o) "Director" means a member of the Board or the board of directors of any Related Entity.

(p) "Disability" means that a Grantee is permanently unable to carry out the responsibilities and functions of the position held by the Grantee by reason of any medically determinable physical or mental impairment. A Grantee will not be considered to have incurred a Disability unless he or she furnishes proof of such impairment sufficient to satisfy the Administrator in its discretion.

(q) "Dividend Equivalent Right" means a right entitling the Grantee to compensation measured by dividends paid with respect to Common Stock.

(r) "Employee" means any person, including an Officer or Director, who is an employee of the Company or any Related Entity. The payment of a director's fee by the Company or a Related Entity shall not be sufficient to constitute "employment" by the Company.

(s) "Exchange Act" means the Securities Exchange Act of 1934, as amended.

(t) "Fair Market Value" means, as of any date, the value of Common Stock determined as follows: (i) Where there exists a public market for the Common Stock, the Fair Market Value shall be (A) the closing price for a Share for the last market trading day prior to the time of the determination (or, if no closing price was reported on that date, on the last trading date on which a closing price was reported) on the stock exchange or national market system determined by the Administrator to be the primary market for the Common Stock, or (B) if the Common Stock is not traded on any such exchange or national market system, the average of the closing bid and asked prices of a share on the OTC Bulletin Board or other inter-dealer quotation service for the day prior to the time of the determination (or, if no such prices were reported on that date, on the last date on which such prices were reported), in each case, as reported in The Wall Street Journal or such other source as the Administrator deems reliable; or (ii) in the absence of an established market for the Common Stock of the type described in subparagraph (i), above, the Fair Market Value shall be determined by the Administrator in good faith.

(u) "Grantee" means an Employee, Director or Consultant who receives an Award pursuant to an Award Agreement under the Plan.

(v) "Incentive Stock Option" means an Option intended to qualify as an incentive stock option within the meaning of Section 422 of the Code.

(w) "Non-Qualified Stock Option" means an Option not intended to qualify as an Incentive Stock Option.

(x) "Officer" means a person who is an officer of the Company or a Related Entity within the meaning of Section 16 of the Exchange Act and the rules and regulations promulgated thereunder.

(y) "Option" means an option to purchase Shares pursuant to an Award Agreement granted under the Plan.

(z) "Parent" means a "parent corporation", whether now or hereafter existing, as defined in Section 424(e) of the Code.

(aa) "Performance Shares" means Shares or an Award denominated in Shares which may be earned in whole or in part upon attainment of performance criteria established by the Administrator.

(bb) "Performance Units" means an Award which may be earned in whole or in part upon attainment of performance criteria established by the Administrator and which may be settled for cash, Shares or other securities or a combination of cash, Shares or other securities as established by the Administrator.

(cc) "Plan" means this 2016 Equity Incentive Plan.

(dd) "Related Entity" means any Parent, Subsidiary and any business, corporation, partnership, limited liability company or other entity in which the Company, a Parent or a Subsidiary holds a substantial ownership interest, directly or indirectly.

(ee) "Restricted Stock" means Shares issued under the Plan to the Grantee for such consideration, if any, and subject to such restrictions on transfer, rights of first refusal, repurchase provisions, forfeiture provisions, and other terms and conditions as established by the Administrator.

(ff) "Rule 16b-3" means Rule 16b-3 promulgated under the Exchange Act or any successor thereto.

(gg) "SAR" means a stock appreciation right entitling the Grantee to Shares or cash compensation, as established by the Administrator, measured by appreciation in the value of Common Stock.

(hh) "Share" means a share of the Common Stock.

(ii) "Subsidiary" means a "subsidiary corporation", whether now or hereafter existing, as defined in Section 424(f) of the Code.

(jj) "Related Entity Disposition" means the sale, distribution or other disposition by the Company of all or substantially all of the Company's interests in any Related Entity effected by a sale, merger or consolidation or other transaction involving that Related Entity or the sale of all or substantially all of the assets of that Related Entity.

3. Stock Subject to the Plan.

(a) Subject to the provisions of Section 10, below, the maximum aggregate number of Shares which may be issued pursuant to all Awards (including Incentive Stock Options) is 350,000 Shares. The Shares to be issued pursuant to Awards may be authorized, but unissued, or reacquired Common Stock.

(b) Any Shares covered by an Award (or portion of an Award) which is forfeited or canceled, expires or is settled in cash, shall be deemed not to have been issued for purposes of determining the maximum aggregate number of Shares which may be issued under the Plan. If any unissued Shares are retained by the Company upon exercise of an Award in order to satisfy the exercise price for such Award or any withholding taxes due with respect to such Award, such retained Shares subject to such Award shall become available for future issuance under the Plan (unless the Plan has terminated). Shares that actually have been issued under the Plan pursuant to an Award shall not be returned to the Plan and shall not become available for future issuance under the Plan, except that if unvested Shares are forfeited, or repurchased by the Company at their original purchase price, such Shares shall become available for future grant under the Plan.

4. Administration of the Plan.

(a) Plan Administrator.

(i) Administration with Respect to Directors and Officers. With respect to grants of Awards to Directors or Employees who are also Officers or Directors of the Company, the Plan shall be administered by (A) the Board or (B) a Committee designated by the Board, which Committee shall be constituted in such a manner as to satisfy the Applicable Laws and to permit such grants and related transactions under the Plan to be exempt from Section 16(b) of the Exchange Act in accordance with Rule 16b-3. Once appointed, such Committee shall continue to serve in its designated capacity until otherwise directed by the Board.

(ii) Administration with Respect to Consultants and Other Employees. With respect to grants of Awards to Employees or Consultants who are neither Directors nor Officers of the Company, the Plan shall be administered by (A) the Board or (B) a Committee designated by the Board, which Committee shall be constituted in such a manner as to satisfy the Applicable Laws. Once appointed, such Committee shall continue to serve in its designated capacity until otherwise directed by the Board. The Board may authorize one or more Officers to grant such Awards and may limit such authority as the Board determines from time to time. Except for the power to amend the Plan as provided in Section 13 and except for determinations regarding Employees who are subject to Section 16 of the Exchange Act or certain key Employees who are, or may become, as determined by the Board or the Committee, subject to Section 162(m) of the Code compensation deductibility limit, and except as may otherwise be required under applicable stock exchange rules, the Board or the Committee may delegate any or all of its duties, powers and authority under the Plan pursuant to such conditions or limitations as the Board or the Committee may establish to any Officer or Officers of the Company.

(iii) Administration Errors. In the event an Award is granted in a manner inconsistent with the provisions of this subsection, such Award shall be presumptively valid as of its grant date to the extent permitted by Applicable Laws.

(b) Powers of the Administrator. Subject to Applicable Laws and the provisions of the Plan (including any other powers given to the Administrator hereunder), and except as otherwise provided by the Board, the Administrator shall have the authority, in its discretion:

(i) to select the Employees, Directors and Consultants to whom Awards may be granted from time to time hereunder;

(ii) to determine whether and to what extent Awards are granted hereunder;

(iii) to determine the number of Shares or the amount of other consideration to be covered by each Award granted hereunder;

(iv) to approve forms of Award Agreements for use under the Plan;

(v) to determine the terms and conditions of any Award granted hereunder;

(vi) to amend the terms of any outstanding Award granted under the Plan, provided that any amendment that would adversely affect the Grantee's rights under an outstanding Award shall not be made without the Grantee's written consent;

(vii) to construe and interpret the terms of the Plan and Awards granted pursuant to the Plan, including without limitation, any notice of Award or Award Agreement, granted pursuant to the Plan;

(viii) to establish additional terms, conditions, rules or procedures to accommodate the rules or laws of applicable foreign jurisdictions and to afford Grantees favorable treatment under such laws; provided, however, that no Award shall be granted under any such additional terms, conditions, rules or procedures with terms or conditions which are inconsistent with the provisions of the Plan; and

(ix) to take such other action, not inconsistent with the terms of the Plan, as the Administrator deems appropriate.

(c) Effect of Administrator's Decision. All decisions, determinations and interpretations of the Administrator shall be conclusive and binding on all persons.

5. Eligibility, Awards other than Incentive Stock Options may be granted to Employees, Directors and Consultants. Incentive Stock Options may be granted only to Employees of the Company, a Parent or a Subsidiary. An Employee, Director or Consultant who has been granted an Award may, if otherwise eligible, be granted additional Awards. Awards may be granted to Employees, Directors or Consultants who are residing in foreign jurisdictions.

6. Terms and Conditions of Awards.

(a) Type of Awards. The Administrator is authorized under the Plan to award any type of arrangement to an Employee, Director or Consultant that is not inconsistent with the provisions of the Plan and that by its terms involves or might involve the issuance of (i) Shares, (ii) an Option, a SAR or similar right with a fixed or variable price related to the Fair Market Value of the Shares and with an exercise or conversion privilege related to the passage of time, the occurrence of one or more events, or the satisfaction of performance criteria or other conditions, or (iii) any other security with the value derived from the value of the Shares. Such awards include, without limitation, Options, SARs, sales or bonuses of Restricted Stock, Dividend Equivalent Rights, Performance Units or Performance Shares, and an Award may consist of one such security or benefit, or two (2) or more of them in any combination or alternative.

(b) Designation of Award. Each Award shall be designated in the Award Agreement. In the case of an Option, the Option shall be designated as either an Incentive Stock Option or a Non-Qualified Stock Option. However, notwithstanding such designation, to the extent that the aggregate Fair Market Value of Shares subject to Options designated as Incentive Stock Options which become exercisable for the first time by a Grantee during any calendar year (under all plans of the Company or any Parent or Subsidiary) exceeds \$100,000, such excess Options, to the extent of the Shares covered thereby in excess of the foregoing limitation, shall be treated as Non-Qualified Stock Options. For this purpose, Incentive Stock Options shall be taken into account in the order in which they were granted, and the Fair Market Value of the Shares shall be determined as of the date the Option with respect to such Shares is granted.

(c) Conditions of Award. Subject to the terms of the Plan, the Administrator shall determine the provisions, terms, and conditions of each Award including, but not limited to, the Award vesting schedule, repurchase provisions, rights of first refusal, forfeiture provisions, form of payment (cash, Shares, or other consideration, including cashless exercise) upon settlement of the Award, payment contingencies, and satisfaction of any performance criteria. The performance criteria established by the Administrator may be based on any one of, or combination of, increase in share price, earnings per share, total stockholder return, return on equity, return on assets, return on investment, net operating income, cash flow, revenue, economic value added, personal management objectives, or other measure of performance selected by the Administrator. Partial achievement of the specified criteria may result in a partial payment or vesting as specified in the Award Agreement.

(d) Acquisitions and Other Transactions. The Administrator may issue Awards under the Plan in settlement, assumption or substitution for, outstanding awards or obligations to grant future awards in connection with the Company or a Related Entity acquiring another entity, an interest in another entity or an additional interest in a Related Entity whether by merger, stock purchase, asset purchase or other form of transaction.

(e) Deferral of Award Payment. The Administrator may establish one or more programs under the Plan to permit selected Grantees the opportunity to elect to defer receipt of consideration upon exercise of an Award, satisfaction of performance criteria, or other event that absent the election would entitle the Grantee to payment or receipt of Shares or other consideration under an Award. The Administrator may establish the election procedures, the timing of such elections, the mechanisms for payments of, and accrual of interest or other earnings, if any, on amounts, Shares or other consideration so deferred, and such other terms, conditions, rules and procedures that the Administrator deems advisable for the administration of any such deferral program.

(f) Award Exchange Programs. The Administrator may establish one or more programs under the Plan to permit selected Grantees to exchange an Award under the Plan for one or more other types of Awards under the Plan on such terms and conditions as determined by the Administrator from time to time.

(g) Separate Programs. The Administrator may establish one or more separate programs under the Plan for the purpose of issuing particular forms of Awards to one or more classes of Grantees on such terms and conditions as determined by the Administrator from time to time.

(h) Early Exercise. The Award Agreement may, but need not, include a provision whereby the Grantee may elect at any time while an Employee, Director or Consultant to exercise any part or all of the Award prior to full vesting of the Award. Any unvested Shares received pursuant to such exercise may be subject to a repurchase right in favor of the Company or a Related Entity or to any other restriction the Administrator determines to be appropriate.

(i) Term of Award. The term of each Award shall be the term stated in the Award Agreement, provided, however, that the term of an Incentive Stock Option shall be no more than ten (10) years from the date of grant thereof. However, in the case of an Incentive Stock Option granted to a Grantee who, at the time the Option is granted, owns stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary, the term of the Incentive Stock Option shall be five (5) years from the date of grant thereof or such shorter term as may be provided in the Award Agreement.

(j) Transferability of Awards. Except as otherwise provided in this Section, all Awards under the Plan shall be nontransferable and shall not be assignable, alienable, saleable or otherwise transferable by the Grantee other than by will or the laws of descent and distribution except pursuant to a domestic relations order entered by a court of competent jurisdiction. Notwithstanding the preceding sentence, the Board or the Committee may provide that any Award of Non-Qualified Stock Options may be transferable by the recipient to family members or family trusts established by the Grantee. The Board or the Committee may also provide that, in the event that a Grantee terminates employment with the Company to assume a position with a governmental, charitable, educational or similar non-profit institution, a third party, including but not limited to a "blind" trust, may be authorized by the Board or the Committee to act on behalf of and for the benefit of the respective Grantee with respect to any outstanding Awards. Except as otherwise provided in this Section, during the life of the Grantee, Awards under the Plan shall be exercisable only by him or her except as otherwise determined by the Board or the Committee. In addition, if so permitted by the Board or the Committee, a Grantee may designate a beneficiary or beneficiaries to exercise the rights of the Grantee and receive any distributions under the Plan upon the death of the Grantee.

(k) Time of Granting Awards. The date of grant of an Award shall for all purposes be the date on which the Administrator makes the determination to grant such Award, or such other date as is determined by the Administrator. Notice of the grant determination shall be given to each Employee, Director or Consultant to whom an Award is so granted within a reasonable time after the date of such grant.

7. Award Exercise or Purchase Price, Consideration, Taxes and Reload Options.

(a) Exercise or Purchase Price. The exercise or purchase price, if any, for an Award shall be as follows:

(i) In the case of an Incentive Stock Option: (A) granted to an Employee who, at the time of the grant of such Incentive Stock Option owns stock representing more than ten percent (10%) of the voting power of all classes of stock of the Company or any Parent or Subsidiary, the per Share exercise price shall be not less than one hundred ten percent (110%) of the Fair Market Value per Share on the date of grant; or (B) granted to any Employee other than an Employee described in the preceding clause, the per Share exercise price shall be not less than one hundred percent (100%) of the Fair Market Value per Share on the date of grant.

(ii) In the case of a Non-Qualified Stock Option, the per Share exercise price shall be not less than one hundred percent (100%) of the Fair Market Value per Share on the date of grant unless otherwise determined by the Administrator.

(iii) In the case of other Awards, such price as is determined by the Administrator.

(iv) Notwithstanding the foregoing provisions of this Section 7(a), in the case of an Award issued pursuant to Section 6(d), above, the exercise or purchase price for the Award shall be determined in accordance with the principles of Section 424(a) of the Code.

(b) Consideration. Subject to Applicable Laws, the consideration to be paid for the Shares to be issued upon exercise or purchase of an Award including the method of payment, shall be determined by the Administrator (and, in the case of an Incentive Stock Option, shall be determined at the time of grant). In addition to any other types of consideration the Administrator may determine, the Administrator is authorized to accept as consideration for Shares issued under the Plan the following, provided that the portion of the consideration equal to the par value of the Shares must be paid in cash or other legal consideration permitted by the applicable laws of the jurisdiction in which the Company is then incorporated.

(i) cash;

(ii) check;

(iii) delivery of Grantee's promissory note with such recourse, interest, security, and redemption provisions as the Administrator determines is appropriate;

(iv) surrender of Shares or delivery of a properly executed form of attestation of ownership of Shares as the Administrator may require including withholding of Shares otherwise deliverable upon exercise of the Award) which have a Fair Market Value on the date of surrender or attestation equal to the aggregate exercise price of the Shares as to which said Award shall be exercised (but only to the extent that such exercise of the Award would not result in an accounting compensation charge with respect to the Shares used to pay the exercise price unless otherwise determined by the Administrator);

(v) with respect to options, payment through a broker-dealer sale and remittance procedure pursuant to which the Grantee (A) shall provide written instructions to a Company designated brokerage firm to effect the immediate sale of some or all of the purchased Shares and remit to the Company, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased Shares and (B) shall provide written directives to the Company to deliver the certificates for the purchased Shares directly to such brokerage firm in order to complete the sale transaction; or

(vi) with respect to options provided there is then an established market for the Common Stock, by a "cashless exercise" as a result of which the Grantee shall be entitled to receive that number of shares of Common Stock equal to the quotient of (i) the number of Options surrendered for exercise and (ii) the difference between the Fair Market Value (determined in accordance with clause (i) of Section 2(t) hereof) and the exercise price of the Option, in which case the number of Options surrendered for exercise shall be cancelled;

(vii) any combination of the foregoing methods of payment.

(c) Taxes. No Shares shall be delivered under the Plan to any Grantee or other person until such Grantee or other person has made arrangements acceptable to the Administrator for the satisfaction of any foreign, federal, state, or local income and employment tax withholding obligations, including, without limitation, obligations incident to the receipt of Shares or the disqualifying disposition of Shares received on exercise of an Incentive Stock Option. Upon exercise of an Award, the Company shall withhold or collect from Grantee an amount sufficient to satisfy such tax obligations.

(d) Reload Options. In the event the exercise price or tax withholding of an Option is satisfied by the Company or the Grantee's employer withholding Shares otherwise deliverable to the Grantee, the Administrator may issue the Grantee an additional Option, with terms identical to the Award Agreement under which the Option was exercised, but at an exercise price as determined by the Administrator in accordance with the Plan.

8. Exercise of Award.

(a) Procedure for Exercise; Rights as a Stockholder.

(i) Any Award granted hereunder shall be exercisable at such times and under such conditions as determined by the Administrator under the terms of the Plan and specified in the Award Agreement.

(ii) An Award shall be deemed to be exercised upon the later of (x) receipt by the Company of written notice of such exercise in accordance with the terms of the Award by the person entitled to exercise the Award and (y) full payment for the Shares with respect to which the Award is exercised, including, to the extent selected, use of the broker-dealer sale and remittance procedure to pay the purchase price as provided in Section 7(b)(v).

(iii) Until the issuance (as evidenced by the appropriate entry on the books of the Company or of a duly authorized transfer agent of the Company) of the stock certificate evidencing such Shares, no right to vote or receive dividends or any other rights as a stockholder shall exist with respect to Shares subject to an Award, notwithstanding the exercise of an Option or other Award. The Company shall issue (or cause to be issued) such stock certificate promptly upon exercise of the Award. No adjustment will be made for a dividend or other right for which the record date is prior to the date the stock certificate is issued, except as provided in the Award Agreement or Section 10, below.

(b) Exercise of Award Following Termination of Continuous Service.

(i) An Award may not be exercised after the termination date of such Award set forth in the Award Agreement and may be exercised following the termination of a Grantee's Continuous Service only to the extent provided in the Award Agreement.

(ii) Where the Award Agreement permits a Grantee to exercise an Award following the termination of the Grantee's Continuous Service for a specified period, the Award shall terminate to the extent not exercised on the last day of the specified period or the last day of the original term of the Award, whichever occurs first.

(iii) Any Award designated as an Incentive Stock Option to the extent not exercised within the time permitted by law for the exercise of Incentive Stock Options following the termination of a Grantee's Continuous Service shall convert automatically to a Non-Qualified Stock Option and thereafter shall be exercisable as such to the extent exercisable by its terms for the period specified in the Award Agreement.

(c) Buyout Provisions. The Administrator may at any time offer to buy out for a payment in cash or Shares, an Award previously granted, based on such terms and conditions as the Administrator shall establish and communicate to the Grantee at the time that such offer is made.

9. Conditions Upon Issuance of Shares.

(a) Shares shall not be issued pursuant to the exercise of an Award unless the exercise of such Award and the issuance and delivery of such Shares pursuant thereto shall comply with all Applicable Laws, and shall be further subject to the approval of counsel for the Company with respect to such compliance.

(b) As a condition to the exercise of an Award, the Company may require the person exercising such Award to represent and warrant at the time of any such exercise that the Shares are being purchased only for investment and without any present intention to sell or distribute such Shares if, in the opinion of counsel for the Company, such a representation is required by any Applicable Laws.

10. Adjustments Upon Changes in Capitalization. Subject to any required action by the stockholders of the Company, the Administrator may, in its discretion, proportionately adjust the number of Shares covered by each outstanding Award, and the number of Shares which have been authorized for issuance under the Plan but as to which no Awards have yet been granted or which have been returned to the Plan, the exercise or purchase price of each such outstanding Award, as well as any other terms that the Administrator determines require adjustment for (a) any increase or decrease in the number of issued Shares resulting from a stock split, reverse stock split, stock dividend, combination or reclassification of the Shares, (b) any other increase or decrease in the number of issued Shares effected without receipt of consideration by the Company, or (c) as the Administrator may determine in its discretion, any other transaction with respect to Common Stock to which Section 424(a) of the Code applies; provided, however that conversion of any convertible securities of the Company shall not be deemed to have been "effected without receipt of consideration." Such adjustment shall be made by the Administrator and its determination shall be final, binding and conclusive. Except as the Administrator determines, no issuance by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall affect, and no adjustment by reason hereof shall be made with respect to, the number or price of Shares subject to an Award.

11. Corporate Transactions and Related Entity Dispositions. Except as may be provided in an Award Agreement:

(a) The Administrator shall have the authority, exercisable either in advance of any actual or anticipated Corporate Transaction or Related Entity Disposition or at the time of an actual Corporate Transaction or Related Entity Disposition and exercisable at the time of the grant of an Award under the Plan or any time while an Award remains outstanding, to provide for the full automatic vesting and exercisability of one or more outstanding unvested Awards under the Plan and the release from restrictions on transfer and repurchase or forfeiture rights of such Awards in connection with a Corporate Transaction or Related Entity Disposition, on such terms and conditions as the Administrator may specify. The Administrator also shall have the authority to condition any such Award vesting and exercisability or release from such limitations upon the subsequent termination of the Continuous Service of the Grantee within a specified period following the effective date of the Corporate Transaction or Related Entity Disposition. Effective upon the consummation of a Corporate Transaction or Related Entity Disposition, all outstanding Awards under the Plan, shall remain fully exercisable until the expiration or sooner termination of the Award.

(b) The portion of any Incentive Stock Option accelerated under this Section 11 in connection with a Corporate Transaction or Related Entity Disposition shall remain exercisable as an Incentive Stock Option under the Code only to the extent the \$ 100,000 dollar limitation of Section 422(d) of the Code is not exceeded. To the extent such dollar limitation is exceeded, the accelerated excess portion of such Option shall be exercisable as a Non-Qualified Stock Option.

12. Effective Date and Term of Plan. The Plan shall become effective upon the earlier to occur of its adoption by the Board or its approval by the stockholders of the Company. It shall continue in effect for a term of ten (10) years unless sooner terminated. Subject to Section 13 below, and Applicable Laws, Awards may be granted under the Plan upon its becoming effective.

13. Amendment, Suspension or Termination of the Plan.

(a) The Board may at any time amend, suspend or terminate the Plan. To the extent necessary to comply with Applicable Laws, the Company shall obtain stockholder approval of any Plan amendment in such a manner and to such a degree as required.

(b) No Award may be granted during any suspension of the Plan or after termination of the Plan.

(c) Any amendment, suspension or termination of the Plan (including termination of the Plan under Section 12, above) shall not affect Awards already granted, and such Awards shall remain in full force and effect as if the Plan had not been amended, suspended or terminated, unless mutually agreed otherwise between the Grantee and the Administrator, which agreement must be in writing and signed by the Grantee and the Company.

14. Reservation of Shares.

(a) The Company, during the term of the Plan, will at all times reserve and keep available such number of Shares as shall be sufficient to satisfy the requirements of the Plan.

(b) The inability of the Company to obtain authority from any regulatory body having jurisdiction, which authority is deemed by the Company's counsel to be necessary to the lawful issuance and sale of any Shares hereunder, shall relieve the Company of any liability in respect of the failure to issue or sell such Shares as to which such requisite authority shall not have been obtained.

15. No Effect on Terms of Employment/Consulting Relationship. The Plan shall not confer upon any Grantee any right with respect to the Grantee's Continuous Service, nor shall it interfere in any way with his or her right or the Company's right to terminate the Grantee's Continuous Service at any time, with or without cause.

16. Unfunded Plan. Unless otherwise determined by the Board or the Committee, the Plan shall be unfunded and shall not create (or construed to create) a trust or a separate fund or funds. The Plan shall not establish any fiduciary relationship between the Company and any Grantee or other person. To the extent any person holds any rights by virtue of an Award granted under the Plan, such right (unless otherwise determined by the Board or the Committee) shall be no greater than the right of an unsecured general creditor of the Company.

17. No Effect on Retirement and Other Benefit Plans. Except as specifically provided in a retirement or other benefit plan of the Company or a Related Entity, Awards shall not be deemed compensation for purposes of computing benefits or contributions under any retirement plan of the Company or a Related Entity, and shall not affect any benefits under any other benefit plan of any kind or any benefit plan subsequently instituted under which the availability or amount of benefits is related to level of compensation. The Plan is not a "Retirement Plan" or "Welfare Plan" under the Employee Retirement Income Security Act of 1974, as amended.

18. Stockholder Approval. The grant of Incentive Stock Options under the Plan shall be subject to approval by the stockholders of the Company within twelve (12) months before or after the date the Plan is adopted by the Board excluding Incentive Stock Options issued in substitution for outstanding Incentive Stock Options pursuant to Section 424(a) of the Code. Such stockholder approval shall be obtained in the degree and manner required under Applicable Laws. The Administrator may grant Incentive Stock Options under the Plan prior to approval by the stockholders, but until such approval is obtained, no such Incentive Stock Option shall be exercisable. In the event that stockholder approval is not obtained within the twelve (12) month period provided above, all Incentive Stock Options previously granted under the Plan shall be exercisable as Non-Qualified Stock Options.

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO RULE 13a-14(a) UNDER THE EXCHANGE ACT

I, Daniel R. Godin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Air Industries Group;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: November 14, 2016

/s/ Daniel R. Godin

Daniel R. Godin

Chief Executive Officer (Principal Executive Officer)

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO RULE 13a-14(a) UNDER THE EXCHANGE ACT

I, Michael Recca, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Air Industries Group;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Dated: November 14, 2016

/s/ Michael Recca

Michael Recca

Chief Financial Officer (Principal Financial Officer)

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
(18 U.S.C. SECTION 1350)

In connection with the Quarterly Report of Air Industries Group, a Nevada corporation (the "Company"), on Form 10-Q for the quarter ended September 30, 2016, as filed with the Securities and Exchange Commission (the "Report"), Daniel R. Godin, Chief Executive Officer of the Company, does hereby certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. ss. 1350), that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Dated: November 14, 2016

/s/ Daniel R. Godin

Daniel R. Godin

Chief Executive Officer (Principal Executive Officer)

[A signed original of this written statement required by Section 906 has been provided to Air Industries Group and will be retained by Air Industries Group and furnished to the Securities and Exchange Commission or its staff upon request.]

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002
(18 U.S.C. SECTION 1350)

In connection with the Quarterly Report of Air Industries Group, a Nevada corporation (the "Company"), on Form 10-Q for the quarter ended September 30, 2016, as filed with the Securities and Exchange Commission (the "Report"), Michael Recca, Chief Financial Officer of the Company, does hereby certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. ss. 1350), that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

Dated: November 14, 2016

/s/ Michael Recca

Michael Recca

Chief Financial Officer (Principal Financial Officer)

[A signed original of this written statement required by Section 906 has been provided to Air Industries Group and will be retained by Air Industries Group and furnished to the Securities and Exchange Commission or its staff upon request.]