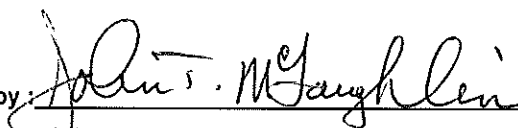


AD ASTRA ROCKET COMPANY (A DEVELOPMENT STAGE ENTERPRISE)

(UNAUDITED)

**CONSOLIDATED FINANCIAL STATEMENTS
as of and for the period ending September 30, 2012, the
year ended December 31, 2011 and the period from Inception,
July 15, 2005, to September 30, 2012**

Prepared by:


John T McLaughlin Financial Manager

Date: October 25, 2012

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	<u>Page</u>
Consolidated Financial Statements:	
Consolidated Balance Sheets as of September 30, 2012 and December 31, 2011	3
Consolidated Statements of Operations for the periods ended September 30, 2012, December 31, 2011 and for the period from inception, July 15, 2005 to September 30, 2012	4
Consolidated Statements of Changes in Stockholders' Equity/ (Deficit) for the period ended September 30, 2012 and for the period from inception, July 15, 2005 to September 30, 2012	5
Consolidated Statements of Cash Flows for the periods ended September 30, 2012, December 31, 2011 and for the period from inception, July 15, 2005 to September 30, 2012	7
Notes to Consolidated Financial Statements	8

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

September 30, 2012 and December 31, 2011

ASSETS	Sep 30, 2012	Dec 31, 2011
Current Assets:		
Cash	14,655	14,822
Accounts receivable, Net	103,768	18,139
Prepaid expenses	11,241	12,701
Total current assets	129,664	45,662
Other Assets	68,730	71,443
Property and equipment, net	301,450	933,243
Capital lease assets, net	17,205	41,160
Total assets	517,049	1,091,508
LIABILITIES AND STOCKHOLDERS' (DEFICIT)/EQUITY		
Current liabilities		
Line of credit, related party	408,000	408,000
Line of credit, bank	250,000	-
Notes payable, bank	200,000	-
Notes payable, related party	75,051	175,051
Short-term portion deferred lease expense	-	18,442
Short-term portion capital lease obligation	4,058	29,852
Bonds payable	-	100,000
Accounts payable	380,273	553,896
Accounts payable, related party	199,893	200,671
Accrued liabilities	470,054	324,197
Interest payable to related party	63,840	56,795
Total current liabilities	2,051,169	1,866,904
Long-term liabilities:		
Long-term portion deferred lease expense	-	-
Long-term portion capital lease obligation	10,632	10,632
Total long-term liabilities	10,632	10,632
Total liabilities	2,061,801	1,877,536
Commitments and contingencies		
Stockholders' (deficit)/equity:		
Preferred Stock:		
Series A, par value \$0.01, 2,200 shares authorized; 369 shares issued and outstanding	4	4
Series B, par value \$0.01, 1,000 shares authorized; none issued or outstanding	-	-
Series C, par value \$0.01, 1,000 shares authorized; 25 issued and outstanding	-	-
Common stock par value \$0.01, 75,000,000 shares authorized; 20,424,448 and 20,251,645 shares issued and outstanding	204,345	202,517
Additional paid in Capital	29,590,815	27,863,402
Losses accumulated during developmental stage	(31,339,916)	(28,851,951)
Total stockholders' (deficit)/equity	(1,544,752)	(786,028)
Total liabilities and stockholders' (deficit)/equity	517,049	1,091,508

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

for the periods ended September 30, 2012, December 31, 2011 and for the
period from inception, July 15, 2005, to September 30, 2012

	September 31, 2012	December 31, 2011	Period from Inception, July 15, 2005, to Sept 30, 2012
General and administrative expenses:			
Payroll expense	\$ 1,568,635	\$ 2,287,649	\$ 16,077,331
Professional fees	49,509	52,633	1,562,564
Other general and administrative expenses	<u>1,472,275</u>	<u>2,347,158</u>	<u>14,757,848</u>
Total general and administrative expenses	3,090,419	4,687,440	32,397,743
Other income (expense)			
Interest income	13	83	324,078
Interest expense	(15,761)	(25,657)	(1,146,120)
Other income	<u>618,958</u>	<u>435,589</u>	<u>1,880,625</u>
Total other income (expense), net	<u>603,210</u>	<u>410,015</u>	<u>1,058,583</u>
Net loss before provision for income taxes	(2,487,210)	(4,277,425)	(31,339,161)
Provision for income taxes	<u>-</u>	<u>-</u>	<u>-</u>
Net loss	\$ <u>(2,487,210)</u>	\$ <u>(4,277,425)</u>	\$ <u>(31,339,161)</u>
Basic and dilute loss per share	\$ <u>(0.12)</u>	\$ <u>(0.21)</u>	\$ <u>(1.86)</u>
Basic and diluted weighted-average shares outstanding	<u>20,434,071</u>	<u>20,164,163</u>	<u>16,876,015</u>

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (DEFICIT)

for the Period ending Sep 30, 2012

	Preferred Stock				Common Stock				Stock	Additional	Accumulated	Total
	Series A		Series B		Class A		Class B		Subscription	Paid-in	Deficit	Stockholders
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Receivable	Capital	During Development	Equity (Deficit)
Balance as of July 15, 2005												
Common Stock Issued for Cash							3,500	4		49,996		50,000
Additional Capital Contributed by Stockholder										2,000		2,000
Common Stock Issued for Services							762			10,885		10,885
Net Loss											(881,852)	(881,852)
Balance as of December 31, 2005							4,262	4		62,881	(881,852)	(818,967)
Common Stock Issued for Cash							100	1		499,999		500,000
Preferred Stock Issued for Cash	809	1								4,044,999		4,045,000
Preferred Stock Subscribed For	111								(1,387,500)	1,387,500		0
Compensatory Element of Stock Option Grant										312,764		312,764
Net Loss											(3,489,603)	(3,489,603)
Balance as of December 31, 2006	920	1					4,362	5	(1,387,500)	6,308,143	(4,371,455)	549,194
Common Stock Issued for Cash												0
Preferred Stock Issued for Cash	198									2,741,302		2,741,302
Preferred Stock Subscribed For									1,387,500			1,387,500
Compensatory Element of Stock Option Grant										30,987		30,987
Net Loss											(4,713,110)	(4,713,110)
Balance as of December 31, 2007	1,118	1					4,362	5	0	9,080,432	(9,084,565)	(4,127)
Common Stock Issued for Cash					71		3,000	3		1,419,997		1,420,000
Preferred Stock Issued for Cash	68									1,216,000		1,216,000
Preferred Stock Converted to Common Stock	(857)	0	0	0	857	0	0	0	0	0	0	0
Stock Dividends					2,780,072	2,781	13,081,638	13,081		(15,862)		0
Compensatory Element of Stock Option Grant										140,388	0	140,388
Net Loss											(5,704,402)	(5,704,402)
Balance as of December 31, 2008	329	1			2,781,000	2,781	13,089,000	13,089	0	11,840,955	(14,788,967)	(2,932,141)
Common Stock Issued for Cash					160,548	160	3,000	3		1,114,984		1,115,147
Preferred Stock Issued for Cash	23		36							1,195,020		1,195,020
Preferred Stock Converted to Common Stock												0
Stock Dividends												0
Compensatory Element of Stock Option Grant										86,219		86,219
Net Loss											(4,961,871)	(4,961,871)
Balance as of December 31, 2009	352	1	36		2,941,548	2,941	13,092,000	13,092	0	14,237,178	(19,750,838)	(5,497,626)

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF STOCKHOLDER'S EQUITY (DEFICIT)

for the Period ending Sep 30, 2012

	Preferred Stock				Common Stock				Stock	Additional	Accumulated	Total
	Series A		Series B						Subscription	Paid-in	Deficit	Stockholders
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Receivable	Capital	During Development	Equity(Deficit)
Consolidate Common Stock Class A & Class B					(2,941,548)	(2,941)	2,941,548	2,941				0
Common Stock Issued for Cash/Net of issuance costs of \$319,396					0	180,504	1,805			1,446,071		1,447,876
Common Stock/Debtenture Conversion*		0			0	3,546,000	3,546			7,013,281		7,016,827
Change in Par Value of Stock Common Stock				0	0		176,217			(176,217)		0
Preferred Stock Issued for Cash 2010 net of issuance costs of \$176,586	0		70	0						1,749,113	0	1,749,113
Preferred Stock Converted to Common Stock			(106)			318,000	3,180			(3,180)		0
Preferred Stock Subscribed For	17	0							0	510,000		510,000
Change in Par Value of Preferred Stock		3								(3)		0
Stock Dividends												0
Compensatory Element of Stock Option Grant										163,144		163,144
Net Loss											(4,823,688)	(4,823,688)
Balance as of December 31, 2010	369	4	0	0	0	0	20,078,052	200,781	0	24,939,386	(24,574,526)	565,644
Common Stock Issued for Cash/Net of issuance costs of \$234,163					0	172,093	1,721			1,756,318		1,758,039
Common stock issued for conversion of convertible debenture, related party						1,500	15			17,985		18,000
Preferred Stock Issued for conversion of vendor payable, related party			3							108,000		108,000
Preferred Stock Issued for conversion of line of credit, related party			22							792,000		792,000
Stock Dividends												0
Compensatory Element of Stock Option Grant										249,713		249,713
Net Loss											(4,277,425)	(4,277,425)
Balance as of December 31, 2011	369	4	25	0	0	0	20,251,645	202,517	0	27,863,402	(28,851,951)	(766,029)
Common Stock Issued for Cash/Net of issuance costs of \$164,779					0	182,426	1,824			1,481,207		1,483,031
Common stock issued for conversion of convertible debenture, related party												0
Preferred Stock Issued for cash			1							36,000		36,000
Preferred Stock Issued for conversion of line of credit, related party												0
Stock Dividends												0
Compensatory Element of Stock Option Grant										210,211		210,211
Net Loss											(2,487,966)	(2,487,966)
Balance as of Sep 30, 2012	369	4	26	0	0	0	20,434,071	204,341	0	29,590,820	(31,339,917)	(1,544,752)

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF CASH FLOWS
As of Sep 30, 2012, the year ended December 31, 2011 and for the
period from inception July 15, 2005 to September 30, 2012

	Period Ended September 30, 2012	Period Ended December 31, 2011	Period from Inception July 15, 2005 to Sep 30, 2012
Net Loss	(2,487,966)	(4,277,425)	(31,339,917)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization activities	655,748	1,127,880	5,997,752
Compensatory element of stock option grants	210,211	249,713	1,193,426
Common stock issued for services		-	10,885
Deferred salary forgiven		(143,878)	(143,878)
Deferred rent expense	(18,442)	(31,584)	-
Changes in operating assets and liabilities			
Accounts receivable	(85,629)	4,042	(103,769)
Prepaid expenses	1,460	(2,183)	(11,242)
Other assets	2,713	(3,246)	2,613
Accounts payable and accrued liabilities	(213,457)	383,086	633,168
Accounts payable, related party	(778)	778	199,893
Interest payable, related party	41,236	22,604	1,103,974
Deferred salary	151,500	(189,601)	483,727
Net cash used in operating activities	(1,743,404)	(2,859,814)	(21,973,368)
Cash flows used in investing activities:			
Purchase of equipment	-	(13,912)	(6,253,372)
Proceeds from disposal of fixed assets	-	-	25,344
Net cash used in investing activities	-	(13,912)	(6,228,028)
Cash flows from financing activities			
Payments on capital lease obligations	(25,794)	(30,468)	(145,029)
Payments on royalty note payable	-	(7,359)	(20,000)
Payments on notes payable, related party	(200,000)	(21,949)	(221,949)
Payments on bonds payable	-	-	-
Proceeds from:			
Line of Credit	250,000	510,000	1,960,000
Notes payable, related party	-	197,000	197,000
Short term notes payable	200,000	-	200,000
Issuance of convertible debentures	-	-	6,000,000
Capital contribution by stockholder	-	-	2,000
Issuance of bonds payable	-	100,000	100,000
Stockholder subscription receivable	-	-	1,387,500
Issuance of common stock, net of issuance costs	1,483,031	1,758,039	7,774,093
Issuance of preferred stock, net of issuance costs	36,000		10,982,436
Net proceeds provided by financing activities	1,743,237	2,505,263	28,216,051
Net (decrease) increase in cash and cash equivalents	(167)	(368,463)	14,655
Cash and cash equivalents, beginning of period	14,822	383,285	-
Cash and cash equivalents, end of period	14,655	14,822	14,655

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

1. Summary of Significant Accounting Policies

Ad Astra Rocket Company and Subsidiary (the "Company" or "AARC") is a development stage enterprise incorporated on January 14, 2005 and officially organized on July 15, 2005 in Houston, Texas. The Company is considered a development stage enterprise because it has not yet generated significant revenue from sale of its products and has devoted substantially all of its efforts in raising capital to develop its products to bring to market. The Company is dedicated to the research and development of advanced plasma rocket propulsion technology and is continuing with development of the Variable Specific Impulse Magnetoplasma ("VASIMR") and its associated technologies. The Company is also involved in furthering the technology for the usage of plasma in other areas such as medical waste.

Basis of Consolidation

The consolidated financial statements include the accounts of the Company's direct, wholly owned subsidiaries: Ad Astra Rocket Company (Costa Rica) S.R.L. incorporated in Costa Rica, and Ad Astra Servicios Energeticos Y Ambientales, Inc. a Delaware corporation. The consolidated financial statements also include the accounts of the Company's indirect, wholly owned subsidiary Ad Astra Servicios Energeticos y Ambientales AASEA, S.R.L., a Costa Rican corporation which is a direct, wholly owned subsidiary of Ad Astra Servicios Energéticos Y Ambientales, Inc. All significant intercompany accounts and transactions have been eliminated in consolidation.

The financial position, results of operations and cash flows of the Company's foreign subsidiary are determined using the United States of America dollar as the functional currency.

Financial Accounting Standards Board ("FASB") Codification

In June 2009, the FASB issued Statement of Financial Accounting Standards ("SFAS") No. 168, "The FASB Accounting Standards Codification TM and the Hierarchy of Generally Accepted Accounting Principles - a replacement of FASB Statement No. 162" ("SFAS 168"). The FASB Accounting Standards Codification TM, ("Codification" or "ASC") became the source of authoritative GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of SFAS 168, the Codification superseded all then-existing non-SEC accounting and reporting standards. All other non-grandfathered non-SEC accounting literature not included in the Codification became non-authoritative.

Following SFAS 168, the FASB will no longer issue new standards in the form of Statements, FASB Staff Positions, FASB Interpretations, or Emerging Issues Task Force Abstracts; instead, it will issue Accounting Standards Updates ("ASUs"). The FASB will not consider ASUs as authoritative in their own right; rather, these updates will serve only to update the Codification, provide background information about the guidance, and provide the bases for conclusions on the change(s) in the Codification. SFAS No. 168 is incorporated in ASC Topic 105, Generally Accepted Accounting Principles. The Company adopted SFAS No. 168 in the second quarter of 2009, and the Company will provide reference in its consolidated financial statements to both the Codification topic reference and the previously authoritative references related to Codification topics and subtopics, as appropriate.

Cash and Cash Equivalents

For purposes of reporting cash flows, the Company considers all short-term investments with an original maturity of three months or less to be cash equivalents.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities. These estimates also affect disclosure of contingent assets and liabilities at the date of the financial statements and the related reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Management believes that its estimates are reasonable.

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies, continued

Property and Equipment

Property and equipment are stated at cost. Depreciation of property and equipment is provided using the straight-line method for financial reporting purposes based on the estimated useful lives of the assets as follows:

	<u>Years</u>
Computers and software	3
Laboratory equipment	5
Machine shop equipment	5
Capital lease equipment	5

Expenditures for major renewals and improvements that extend the useful lives of the property and equipment are capitalized. Expenditures for maintenance and repairs are charged to expense as incurred. The cost and accumulated depreciation of assets sold or otherwise disposed of are removed from the accounts and any resulting gain or loss is reflected in operations.

Income Taxes

The Company uses the liability method of accounting for income taxes. Under this method, deferred income taxes are recorded to reflect the tax consequences on future years of temporary differences between the tax basis of assets and liabilities and their financial amounts at year-end. The Company provides a valuation allowance to reduce deferred tax assets to their net realizable value.

The Company uses ASC 740-10, formerly known as Financial Accounting Standard ("FAS") Interpretation No. 48, *"Accounting for Uncertainty in Income Taxes, an Interpretation of FAS No. 109"*, which creates a single model to address uncertainty in income tax positions and prescribes the minimum recognition threshold a taxation is required to meet before recognized in the financial statements. The Company did not recognize any interest or penalties related to any unrecognized tax position during the years ended December 31, 2011 and 2010.

The Company files a separate federal income tax return in the United States and state tax returns where applicable. Because the Company has only been in existence for six years, all tax returns filed during its existence are subject to state and local income tax examinations.

Stock-Based Compensation

ASC 718-10, formerly known as Statement of Financial Accounting Standards No. 123(R) "Accounting for Stock-Based Compensation", requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in the Company's consolidated statement of operations.

The Company adopted ASC 718-10 using the modified prospective transition method, as of January 1, 2006. The Company's consolidated financial statements as of and for the year ended December 31, 2011 and 2010 and for the period from inception, July 15, 2005 to September 30, 2012 reflect the impact of ASC 718-10. In accordance with the modified prospective transition method, the Company's consolidated financial statements for prior periods have not been restated to reflect, and do not include, the impact of ASC 718-10. Stock-based compensation expense recognized under ASC 718-10 for the periods ended September 30, 2012, December 31, 2011 and for the period from inception, July 15, 2005, to September 30, 2012 was \$210,211, \$249,713, and \$1,193,426, respectively, which consists of stock-based compensation expense related to employee and director stock options issuances.

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

1. Summary of Significant Accounting Policies, continued

Concentrations of Credit Risk

The Company maintains its cash in financial institutions selected by management based upon their assessment of the financial stability of the institution. Balances periodically exceed the federal depository insurance limit; however, the Company has not experienced any losses on deposits.

Research and Development

Costs of research and development projects are expensed as incurred. These costs consist of direct costs associated with the design of new products. Research and development expenses for the period ended September 30, 2012, December 31, 2011, and for the period from inception, July 15, 2005, to September 30, 2012 was \$828,163, \$1,396,062, and \$9,975,818.

Fair Value of Financial Instruments

Fair value estimates of financial instruments are based on relevant market information and may be subjective in nature and involve uncertainties and matters of significant judgment. The Company believes that the carrying value of its assets and liabilities approximates the fair value of such items. The Company does not hold or issue financial instruments for trading purposes. The Company adheres to ASC 820 and includes fair value information in the notes to financial statements when the fair value of its financial instruments is different from the book value. When the book value approximates fair value, no additional disclosure is made.

Reclassifications

Certain items in the 2011 consolidated financial statements have been reclassified to conform to the 2012 consolidated financial statements' presentation. The reclassifications have no impact on net loss or stockholders' equity/(deficit) as previously reported.

New Accounting Pronouncements

In January 2010, the FASB issued ASU 2010-06, *Fair Value Measurements and Disclosures (Topic 820) – Improving Disclosures about Fair Value Measurements*, expanding disclosures about fair value measurements by adding disclosures about the different classes of assets and liabilities measured at fair value, the valuation techniques and inputs used, the activity in Level 3 fair value measurements and the transfers between Levels 1, 2 and 3. The new disclosures and clarifications of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosure requirements related to the activity in Level 3 fair value measurements. Those disclosure requirements are effective for fiscal years beginning after December 15, 2010. The Company adopted the new guidance in fiscal 2010, and it did not have an impact on the Company's financial statements.

In May 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update("ASU") No. 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and International Financial Reporting Standards ("IFRS")*. This pronouncement was issued to provide a consistent definition of fair value and ensure that the fair value measurement and disclosure requirements are similar between US GAAP and IFRS. ASU 2011-04 changes certain fair value measurement principles and enhances the disclosure requirements, particularly for Level 3 fair value measurements. ASU No. 2011-04 is effective for reporting periods beginning after December 15, 2011 with application on a prospective basis. The Company does not anticipate the adoption of this new guidance to have a significant impact on its financial statements.

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

In June 2011, the FASB issued ASU No. 2011-05, *Presentation of Comprehensive Income*. ASU 2011-05 requires comprehensive income to be reported in either a single statement or in two consecutive statements reporting net income and other comprehensive income. The ASU does not change what is required to be reported in other comprehensive income or the requirement to disclose reclassifications of items from other comprehensive income to net income. In addition, in December 2011, the FASB issued ASU 2011-12 *Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05*. ASU 2011-12 indefinitely defers the provision in ASU 2011-05 under which entities must present reclassification adjustments out of accumulated other comprehensive income by component in both the statement where net income is presented and the statement where other comprehensive income is presented. ASU 2011-05 is effective for interim and annual periods beginning after December 31, 2011. Early adoption is permitted but full retrospective application is required. The adoption ASU 2011-05 only impacts financial statement presentation; accordingly, it will have no impact on the Company's financial condition, results of operations, or cash flows.

In December 2011, the FASB issued ASU No. 2011-11, *Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities*. ASU No. 2011-11 was issued to provide enhanced disclosures that will enable users of the financial statements to evaluate the effect or potential effect of netting arrangements on an entity's financial position. The amendments under ASU No. 2011-11 require enhanced disclosures by requiring entities to disclose both gross information and net information about both instruments and transactions subject to an agreement similar to a master netting arrangement. This scope would include derivatives, sale and repurchase agreements, reverse sale and repurchase agreements, and securities borrowing and lending arrangements. ASU No. 2011-11 is effective retrospectively for annual periods beginning on or after January 1, 2013, and interim periods within those periods. The Company is evaluating the potential impact of the adoption of this new guidance on its financial statements.

2. Accounts Receivable

The balance of Accounts Receivable, resulting from various speaking and consulting engagements provided by Company officials and Sponsorships in Costa Rica, as of September 30, 2012 and December 31, 2011 was \$103,768 and \$18,139 respectively. Due to the limited number and valuation of the receivables, a reserve has not been set up for uncollectable accounts.

3. Other Assets

Other assets were comprised of the following at September 30, 2012 and December 31, 2011:

	<u>Sep 30, 2012</u>	<u>Dec. 31, 2011</u>
Deposits	\$ 35,068	\$ 35,017
License	33,125	35,000
Other	<u>537</u>	<u>1,426</u>
Total	<u>\$ 68,730</u>	<u>\$ 71,443</u>

The license included in other assets is an intangible asset obtained from a United States of America governmental agency allowing the Company to use certain technologies in the development of its advanced plasma rocket propulsion technology. The license was acquired during 2006 for \$50,000 and is being amortized over 20 years, its contractual life. For the period ended September 30, 2012, December 31, 2011, and the period from inception, July 15, 2005, to September 30, 2012, the Company recorded amortization expense of \$625, \$2,500 and \$16,875 respectively.

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

4. Inventory

The Company is still in the development stage; therefore there is no inventory held resulting in no reserves for obsolescence.

5. Property and Equipment

Property and equipment were comprised of the following at December 31, 2011 and Sep 30, 2012:

<u>Description</u>	<u>2011</u>	<u>Additions/ Transfers in</u>	<u>Retirements/ Transfers out</u>	<u>2012</u>
Computer and software	\$ 569,164	\$ -	\$ -	\$ 569,164
Laboratory equipment	3,828,905	-	-	3,828,905
Machine shop equipment	38,287	-	-	38,287
Leasehold improvements	1,570,963	-	-	1,570,963
Other	138,587	-	-	138,587
	6,145,906	-	-	6,145,906
Less accumulated depreciation	<u>(5,212,663)</u>	<u>(631,793)</u>	<u>-</u>	<u>(5,844,456)</u>
Net property and equipment	<u>\$ 933,243</u>	<u>\$ (631,793)</u>	<u>\$ -</u>	<u>\$ 301,450</u>

Depreciation and amortization expense of \$631,793, \$1,094,957 and \$5,844,456 was recognized during the periods ended September 30, 2012, December 31, 2011 and during the period from inception, July 15, 2005, to September 30, 2012, respectively.

6. Accrued Liabilities

Accrued liabilities were comprised of the following at September 30, 2012 and December 31, 2011:

	<u>2012</u>	<u>2011</u>
Deferred salaries	\$ 298,182	\$ 146,682
Other wages payable	79,137	107,718
Payroll taxes and benefits	92,246	67,812
Other	<u>489</u>	<u>2,525</u>
	<u>\$ 470,054</u>	<u>\$ 567,218</u>

7. Debt Obligations

Line of Credit, Related Party

During the year ended December 31, 2009, the Company entered into an uncollateralized line of credit with a vendor who is owned by a stockholder who is also a member of the board of directors in the amount of \$1,200,000. In May 2011, the Company entered into a note modification agreement which reduced the available line of credit to \$408,000 and extended the maturity date to May 31, 2012. During the year ended December 31, 2011, the vendor converted \$792,000 of the outstanding balance into 22 shares of Series C Preferred stock at \$36,000 per share based on market prices of preferred stock sold to investors through private placements. During the year ended December 31, 2010, this vendor converted \$510,000 of the outstanding balance into 17 shares of Series A Preferred Stock at \$30,000 per share based on market prices of preferred stock sold to investors through private placements. Following these conversions, the Company's outstanding balance at September 30, 2012 and December 31, 2011, on the line of credit was \$408,000 and \$408,000 plus accrued interest of \$63,840 and

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

\$56,795, respectively. All principal and accrued unpaid interest shall be due and payable on or before May 31, 2013. The interest rate on this line of credit is equal to the current "prime" interest rate, 3.25% (as reported by Bloomberg, L.P.) at December 31, 2011.

Notes Payable

The Company had the following short-term debt obligations at September 30, 2012 and December 31, 2011:

	<u>2012</u>	<u>2011</u>
Bonds payable to individual bond holders with principal and interest payable on demand or at month's end from date of issuance. The bonds bear interest at 6%. The Company issued the bonds in October and extended their repayment in each subsequent month through December 2011.	\$ -	\$ 100,000
Revolving line of credit with commercial bank with principal and interest payable no later than May 2013. The note is collateralized and bears a floating annualized interest rate currently at 5.25%.	250,000	-
Notes payable with commercial bank with principal and interest payable in 6 equal monthly installments starting in October 2012. The note is collateralized and bears an annualized interest rate of 9.50%.	200,000	-
Note payable to a related party vendor who is owned by a stockholder and member of the Company's board of directors. The note is uncollateralized, bears no interest, and is due on demand.	-	20,000
Note payable to a related party, the Company's President and Chief Executive Officer, which is due on demand. The note is uncollateralized and bears no interest.	<u>75,051</u>	<u>155,051</u>
Total notes payable	<u>\$ 525,051</u>	<u>\$ 275,051</u>

For the periods ended September 30, 2012 and December 31, 2011, the Company's weighted average interest rate and weighted average effective rate on outstanding short-term debt obligations is 4.51% and 2.40% and 5.25% and 3.25%, respectively.

8. Convertible Debentures

During the period from inception, July 15, 2005, to December 31, 2008, the Company issued \$6 million, of the Company's 4.75% Convertible Debentures ("Debentures"), to the Company's Chairman and Chief Executive Officer. The Debentures were due September 15, 2010, accrue interest at the rate of 4.75% per year and are not collateralized. Interest was payable in full upon maturity on September 15, 2010. All or any portion of the Debentures, including interest accrued thereon, were convertible into shares of the Company's common stock or preferred stock at the option of the holder at any time prior to the maturity date at conversion prices ranging from \$0.95 to \$4.76 per share.

On January 26, 2010, the holder of the convertible debentures elected to convert 100% of the \$6,000,000 outstanding principal and \$1,016,826 of accrued interest into 3,546,000 shares of common stock. The conversion prices for each of the debentures and corresponding interest are as follows:

Debenture	Interest	Conversion
-----------	----------	------------

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

<u>Amount</u>	<u>Income</u>	<u>Price</u>
\$ 1,000,000	\$ 201,768	\$ 0.95
1,000,000	188,051	\$ 0.95
1,000,000	179,203	\$ 1.67
1,000,000	161,634	\$ 3.33
1,000,000	151,743	\$ 4.16
<u>1,000,000</u>	<u>134,427</u>	\$ 4.76
<u>\$ 6,000,000</u>	<u>\$ 1,016,826</u>	

9. Stock Incentive Plan

Effective August 25, 2005 the Company's Board of Directors adopted the Ad Astra Rocket Company 2005 Stock Incentive Plan (the "Plan"). A total of 1,500,000 shares of common stock are reserved for issuance under the Plan. The purpose of the Plan is to provide eligible persons who participate with an opportunity to acquire a proprietary interest in the Company as an incentive for them to remain in the service of the Company. Eligible persons include employees, non-employee members of the Board of Directors, consultants and other independent advisors who provide services to the Company.

The following table summarizes certain information relative to stock options:

	<u>2005 Stock Incentive Plan</u>	
	<u>Shares</u>	<u>Weighted-Average Exercise Price</u>
Outstanding, December 31, 2006	375,000	\$ 1.67
Granted	66,000	4.22
Forfeited/cancelled	<u>-</u>	<u>-</u>
Outstanding, December 31, 2007	441,000	2.05
Granted	18,000	6.67
Forfeited/cancelled	<u>(6,000)</u>	<u>4.17</u>
Outstanding, December 31, 2008	453,000	2.20
Granted	123,000	6.67
Forfeited/cancelled	<u>(54,000)</u>	<u>3.26</u>
Outstanding, December 31, 2009	522,000	3.15
Granted	100,000	10.00
Forfeited/cancelled	<u>(7,500)</u>	<u>6.67</u>
Outstanding, December 31, 2010	614,500	4.22
Granted	-	-
Forfeited/cancelled	(19,500)	7.69
Outstanding, December 31, 2011	<u>591,625</u>	<u>\$ 4.06</u>
Granted	5,000	12.00
Forfeited/cancelled	<u>(35,625)</u>	<u>5.56</u>
Outstanding, September 30, 2012	<u>561,000</u>	<u>\$ 4.00</u>
Exercisable, September 30, 2012	<u>478,750</u>	<u>\$ 3.07</u>

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The weighted-average remaining life and the weighted-average exercise price of all of the options outstanding at September 30, 2012 were 4.9 years and \$4.00, respectively. The exercise prices for the options outstanding at September 30, 2012 ranged from \$1.67 to \$12.00, and information relating to these options is as follows:

<u>Range of Exercise</u>	<u>Stock Options Outstanding</u>	<u>Stock Options Exercisable</u>	<u>Weighted Average Remaining Contract Life</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Exercise Price of Options Exercisable</u>
\$0 - \$1.67	345,000	345,000	3.8 years	\$ 1.67	\$ 1.67
\$4.17	27,000	27,000	4.7 years	\$ 4.17	\$ 4.17
\$6.67	103,500	86,625	6.4 years	\$ 6.67	\$ 6.67
\$10.00 - \$12.00	<u>85,500</u>	<u>20,125</u>	7.8 years	\$ 10.00	\$ 10.12
	<u>561,000</u>	<u>478,750</u>			

The weighted-average estimated fair value of the 5,000 stock options granted pursuant to the Plan during the year ended September 30, 2012 was \$12.00 per share using the Black-Scholes model. These values were calculated using the Black-Scholes model with the following assumptions:

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
Expected volatility	40.0%	-	669.0%	681.0%	415.0%	425.0%	676.0%	-
Risk-free interest rate	2.21%	-	1.15%	1.9%	2.4%	5.01%	5.0%	-
Expected life	10 years	-	10 years	10 years	10 years	10 years	10 years	-

During the period ended September 30, 2012, the Company cancelled 35,625 options for the year ended December 31, 2011 the Company cancelled 19,500 options. The total fair value of options expensed pursuant to the Plan during the period ended September 30, 2012, the 12 months ended December 31, 2011 and for the period from inception, July 15, 2005 through September 30, 2012 were \$210,211, \$249,713, and \$1,193,426 respectively.

As of September 30, 2012, there was approximately \$637,434 of total unrecognized option expense related to non-vested share-based compensation arrangements.

10. Related Party Transactions

For the periods ended September 30, 2012 and December 31, 2011, the Company incurred approximately \$0 and 0, respectively, in legal expenses paid to a director and a stockholder of the Company. During the year ended December 31, 2011, the individual converted \$126,000 of accounts payable into 1,500 shares of Class B Common stock at \$12 per share and 3 shares of Class C Preferred shares at \$36,000. The common stock and preferred stock pricing was consistent with market value purchases of the Company's shares for cash at the time of the conversion. As of September 30, 2012 and December 31, 2011, the Company had a balance outstanding of \$0 and \$0, respectively, related to services rendered by this individual

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

During 2009, the Company entered into a line of credit with a vendor who is owned by a member of the board of directors in the amount of \$1,200,000. On September 30, 2010 this vendor converted \$510,000 of the outstanding balance on this line of credit into seventeen shares of Series A Preferred Stock. Following this conversion and for the periods ended September 30, 2012 and December 31, 2011, the Company's outstanding balance on the line of credit was \$408,000 and \$408,000 plus accrued interest of \$63,840 and \$53,946 respectively. All principal and accrued unpaid interest shall be due and payable on or before the Maturity Date. The "Maturity Date" is currently defined as May 31, 2013. The interest rate on this line of credit is equal to the current "prime" interest rate, 3.25% at September 30, 2012.

In addition this vendor has outstanding balances of \$199,893 and \$199,893 related to systems integration services as of September 30, 2012 and December 31, 2011, respectively. During 2010, the Houston facility temporarily sub-let rental space in its facility to this member of the board. This agreement ended in July 2010. The rental expense for the year 2010 was reduced by \$21,000, as a result of this agreement. There was not an outstanding balance related to this sub-let rental agreement as of December 31, 2010. During the period ended March 31, 2012, the Houston temporarily sub-let rental space in its facility to this member of the board. This agreement ended in August 2012. The rental expense for the year 2012 was reduced by \$21,900, as a result of this agreement. There was not an outstanding balance related to this sub-let agreement as of September 30, 2012.

For the periods ended September 30, 2012 and December 31, 2011, the Company leased its Costa Rica laboratory and warehouse from an investment fund that is controlled by an affiliate of the Company's investment banker and shareholder ("Aldesa"), with lease expenses totaling \$85,016 and \$125,481 respectively. As of September 30, 2012 and December 31, 2011, the Company had an outstanding balance of \$21,713 and \$53,946 respectively with this affiliate. For the periods ended September 30, 2012 and December 31, 2011, the Company paid Aldesa commissions earned in connection with the sale of the Company's stock in the amount of \$164,749 and \$199,388 respectively.

During the year 2010, a contract was entered into by the Company, Costa Rican government, and several small engineering firms in Costa Rica. This contract is funded by the Costa Rican government. The goal of the project is to design and manufacture a mock-up of the platform to house the VASIMR engine on the International Space Station. The total estimated revenue generated by this project will be up to \$216,000, with the Company's proportionate share being approximately \$48,000 in total of which \$15,412 was recorded as other income at December 31, 2011. As of September 30, 2012, a balance of \$0 was recorded in accounts receivable.

11. Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. For the years ended December 31, 2011 and 2010, there were no provisions for income taxes and deferred tax assets have been entirely offset by a valuation allowance, due to the Company's unlikely realization. Significant components of the Company's deferred tax assets and liabilities, at December 31, 2010 and 2009 were as follows:

	<u>2010</u>	<u>2009</u>
Deferred tax assets:		
Net operating loss carry-forwards	\$ 6,413,735	\$ 5,381,000
Non-deductible accruals	356,294	200,046
Basis difference in property and equipment	355,357	128,340
Total deferred tax assets	<u>8,254,354</u>	<u>7,040,897</u>
Valuation allowance	<u>(8,254,354)</u>	<u>(7,040,897)</u>
Net deferred tax asset	<u>\$ -</u>	<u>\$ -</u>

AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The difference between the income tax benefit in the accompanying statements of operations and the amount that would result if the U.S. Federal statutory rate of 34% were applied to pre-tax loss for the years ended December 31, 2011 and 2010 is as follows:

	2011		2010	
	Amount	Percent	Amount	Percent
Benefit for income tax at federal statutory rate	\$(1,454,324)	(34.0)	\$(1,640,053)	(34.0)
Increase in valuation allowance	1,213,457	28.4	1,389,664	28.8
Effect of foreign subsidiary losses	160,744	3.8	206,129	4.3
Conversion of vendor payable to common stock	42,840	1.0	-	-
Compensatory element of stock option grants	84,902	2.0	55,469	1.1
Other	(47,619)	(1.2)	(7,309)	(0.2)
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

As of December 31, 2011, for United States of America ("U.S.") federal income tax reporting purposes, the Company has approximately \$22,184,000 of unused net operating losses ("NOLs") available for carry-forward to future years. The benefit from carry-forward of such NOLs will expire at various dates through December 31, 2031. Because tax laws limit the time during which NOL carry-forwards may be applied against future taxable income, the Company may be unable to take full advantage of its NOL for federal income tax purposes should the Company generate taxable income. Further, the benefit from utilization of NOL carry-forwards could be subject to limitations due to material ownership changes that may or may not occur in the Company. Based on such limitations, the Company has significant NOL's for which realization of tax benefits is uncertain.

12. Equity

Common Stock

The Company's Certificate of Incorporation authorizes the issuance of 75,000,000 shares of Common Stock, par value \$0.01 per share. The Board of Directors has the authority to issue any such shares that are not currently outstanding at such prices and other terms as are approved by the Board. The Company is not party to any agreements with any of its stockholders of any class that gives any such stockholders economic rights related to its shares of capital stock that are not available to all holders of such class of capital stock. In February 2010, the Company amended and restated its Certificate of Incorporation to reflect a change in preferred and common stock par value from \$.001 to \$0.01, and to eliminate its Class A and Class B Common Stock in favor of a single class of Common Stock.

During the year ended December 31, 2008, the Company declared a stock split by way of stock dividend of (1) 3,000 shares of Class A Common Stock for each outstanding share of Class A Common Stock, such that each holder of one share of Class A Common Stock exchanged such share for 3,000 shares of Class A Common Stock and (2) 3,000 shares of Class B Common Stock for each outstanding share of Class B Common Stock, such that each holder of one share of Class B Common Stock exchanged such share for 3,000 shares of Class B Common Stock. The conversion price for each outstanding share of Series A Preferred Stock was adjusted to that each share of Series A Preferred Stock shall be convertible into 3,000 shares of Class A Common Stock. Appropriate adjustments were made for each outstanding option in order to prevent the dilution or enlargement of rights and benefits. As a result, 13,086,000 Class B Common Stock shares and 2,781,000 Class A Common Stock shares were issued in exchange for 4,362 Class B Common Stock shares and 928 Class A Common Stock shares, respectively, outstanding prior to the stock dividend.

On September 28, 2010, the Company received authorization by the Superintendencia General de Valores de Costa Rica (Sugeval) to effect a Restricted Public Offering ("RPO"). This offering was conducted under Costa Rican law outside of the United States. The Company approved the issuance of up to 1,000,000 shares of

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Common Stock pursuant to the Restricted Public Offering, at an offering price of \$10.00 per share. The approval of the RPO by Sugeval resulted in all issued and outstanding shares of Series B Preferred Stock to be converted to Common Stock. This conversion resulted in 106 shares of Preferred Stock Class B being converted into 318,000 shares of Common Stock.

During the year ended December 31, 2010, the Company sold 175,000 shares of Common Stock at a price of \$9.17 and \$10.00 per share resulting in cash proceeds of \$417,272 and \$1,350,000. The Company recorded issuance costs related to these issuances totaling \$319,396 as an offset to additional paid in capital.

During the period ended December 31, 2011, the Company sold 36,450 shares of Common Stock at a price of \$10.00 per share and 135,643 shares of Common Stock at a price of \$12.00 per share, resulting in proceeds of \$1,758,039. The Company recorded issuance costs related to these issuances totaling \$234,163 as an offset to additional paid in capital. The Company also issued 1,500 shares of common stock at a price of \$12.00 per share, to a related party as a settlement for amounts due to the individual for services rendered to the Company.

During the period September 30, 2012, the Company sold 74,164 shares of Common Stock at a price of \$12.00 per share, resulting in proceeds of \$889,218. The Company also sold 108,262 shares of Common Stock at a price of \$7.00, resulting in proceeds of \$756,751. The Company recorded issuance costs related to these issuances totaling \$164,779 as an offset to additional paid in capital.

At September 30, 2012 and December 31, 2011, the company had 20,434,071 and 20,251,645 shares of Common Stock outstanding, respectively. On March 16, 2011 the Board of Directors voted to increase the price of each share of Common Stock from \$10 to \$12 per share. On April 27, 2012 the Board of Directors authorized the Chief Executive Officer to negotiate the best price per share of Common Stock. Subsequent to this authorization the Company sold 108,262 shares of Common Stock at a price of \$7 per share.

Holders of Common Stock are entitled to one vote for each share held and have no preemptive or similar right to subscribe for, or to purchase, any shares of common stock or other securities to be issued by the Company in the future. Holders of shares of Common Stock have no exchange or conversion rights and the shares are not subject to redemption.

Preferred Stock

The Company has 10,000 authorized shares of preferred stock, par value \$0.01 per share. The preferred stock may be issued in series, from time to time, with such designations, rights, preferences, and limitations as the Board of Directors may determine by resolution.

Series A Preferred Stock

At September 30, 2012 and December 31, 2011, the Company had 2,200 and 2,200 shares authorized and 369 and 369 shares issued and outstanding of Series A preferred stock, par value \$0.01 per share ("Series A"), respectively. The Series A has a liquidation preference equal to the original purchase price and does not pay a mandatory dividend. The Series A is convertible into Common Stock any time at the option of the holder at a price determined by dividing the Series A original issue price by the Series A conversion price in effect at the time of conversion. The Series A conversion price is equal to the original issue price per share divided by 3,000. The Company has the right to redeem the Series A for cash at any time after the five year anniversary date of the issuance at a redemption price calculated by multiplying the Series A original issue price by one plus the Prime Rate (as reported by Bloomberg, L.P.) on the date of redemption times the number of years from the applicable Series A original issue date until the date of such calculation with a partial year being expressed by dividing the number of days which have passed since the most recent anniversary by 365, plus all declared but unpaid dividends.

At September 30, 2012 and December 31, 2011 there were no accumulated, undeclared dividends.

Series B Preferred Stock

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

During the year ended December 31, 2008, the Company declared a stock split by way of stock dividend of (1) 3,000 shares of Class A Common Stock for each outstanding share of Class A Common Stock, such that each holder of one share of Class A Common Stock exchanged such share for 3,000 shares of Class A Common Stock and (2) 3,000 shares of Class B Common Stock for each outstanding share of Class B Common Stock, such that each holder of one share of Class B Common Stock exchanged such share for 3,000 shares of Class B Common Stock. The conversion price for each outstanding share of Series A Preferred Stock was adjusted so that each share of Series A Preferred Stock shall be convertible into 3,000 shares of Class A Common Stock. Appropriate adjustments were made for each outstanding option in order to prevent the dilution or enlargement of rights and benefits. As a result, 13,086,000 Class B Common Stock shares and 2,781,000 Class A Common Stock shares were issued in exchange for 4,362 Class B Common Stock shares and 928 Class A Common stock shares, respectively, outstanding prior to the stock split dividend.

At September 30, 2012, December 31, 2011 and December 31, 2010, the Company had 1,000 shares authorized and 0 (zero), 0 (zero) and 36 shares issued and outstanding of Series B Preferred Stock, par value \$0.01 per share ("Series B"), respectively. The Series B has a liquidation preference equal to the original purchase price and does not pay a mandatory dividend. The Series B is convertible by the holder into Common Stock within 15 days of notice of redemption from the Company at a price determined by dividing the Series B original issue price by the Series B conversion price in effect at the time of conversion. The Series B conversion price is equal to the original issue price per share divided by 3,000. The Company has the right to redeem the Series B for cash at any time after the three year anniversary date of the issuance at a redemption price calculated by multiplying the Series B original issue price by one plus the Prime Rate (as reported by Bloomberg, L.P.) on the date of redemption times the number of years from the applicable Series B original issue date until the date of such calculation with a partial year being expressed by dividing the number of days which have passed since the most recent anniversary by 365, plus all declared but unpaid dividends.

During the year ended December 31, 2010, prior to the Common Stock conversion, the Company sold 70 shares of Series B Preferred Stock for proceeds totaling \$2,435,700. The Company recorded issuance costs related to this issuance totaling \$176,586 as an offset to additional paid in capital.

On September 28, 2010, as part of the approval of the RPO in Costa Rica, the 106 shares of issued and outstanding Series B Preferred Stock were automatically converted into 318,000 shares of Common Stock. There were no accumulated or undeclared dividends at the time of conversion on December 31, 2009.

Series C Preferred Stock

At June 30, 2012 and December 31, 2011, the Company had 100 shares authorized and 26 and 25 issued and outstanding, respectively, of Series C Preferred, par value \$0.01 per share ("Series C"). The Series C has a liquidation preference equal to the original purchase price and does not pay a mandatory dividend. The Series C is convertible by the holder into Common Stock within 15 days of notice of redemption from the Company at a price determined by dividing the Series C original issue price by the Series C conversion price in effect at the time of conversion. The Series C conversion price is equal to the original issue price per share divided by 3,000 or \$12 per common share. The Company has the right to redeem the Series C for cash at any time after issuance within twenty days of a written notice at a redemption price equal to the original issue price, plus all declared but unpaid dividends. The Series C stock may become mandatorily convertible to common shares at a conversion rate of 3,000 common stock for each Series C share held in the event of the Company closing the sale of its common stock to the public in an underwritten offering pursuant to an effective registration statement under the Securities Act of 1933, as amended.

During the year ended December 31, 2011, the Company issued 25 shares of Series C Preferred Stock to related parties, who converted \$792,000 of an outstanding line of credit and \$108,000 related to legal services provided by a director to the Company. During the period ending September 30, 2012 the Company issued 1 share of Series C Preferred stock for proceeds of \$36,000. At September 30, 2012 and December 31, 2011, there were no accumulated or undeclared dividends.

13. Commitments

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Operating Leases

In August 2007, the Company entered into a lease agreement for office and laboratory space in Webster, Texas. The term of the agreement was for sixty months with a base rent of \$13,162 per month plus a pro-rata share of operating expenses. There were no payments due during the first twelve months, hence, the Company has accounted for this as a lease incentive and recorded the deferred lease expense asset and corresponding payable on its balance sheet. In July 2008, the Company entered into a lease agreement for additional space for the existing lease entered in August 2007. The term of the agreement is for forty-seven months with a base rent of \$600 per month plus a pro-rata share of operating expenses.

In June 2012, the Company renewed its lease agreement for office and laboratory space in Webster, Texas. The term of the agreement was for 36 months with a base rent of \$8,385 per month for the first year, \$ 11,180 for the second 12 months, and \$13,975 for the final 12 months, plus a pro-rata share of operating expenses. The Company has an option to extend the term of the lease, if certain conditions have been met, for an additional 24 months.

Rent expense for the periods ended September 30, 2012 and December 31, 2011 totaled \$233,489 and \$382,709 respectively, on a straight-line basis. The Company recorded a rent benefit associated with the deferred lease of \$18,442, \$31,584, and \$157,940 for the periods ended September 30, 2012, December 31, 2011 and for the period from inception, July 15, 2005 to September 30, 2012. The remaining deferred lease expense balance at September 30, 2012 and December 31, 2011 was \$0.00 and \$18,442, respectively.

Minimum annual rentals under non-cancelable operating leases of more than one year in duration are as follows:

<u>Year</u>	<u>Annual Expense</u>
2012	25,155
2013	114,595
2014	148,135
2015	<u>97,825</u>
Total	<u>\$ 385,710</u>

Capital Leases

Assets under capital leases are capitalized using the contractual interest rate of 4.75%, for a period of 60 months ending in 2014. Following is an analysis of assets under capital leases at September 30, 2012 and December 31, 2011:

	<u>2012</u>	<u>2011</u>
Machine shop equipment	\$159,719	\$159,719
Less accumulated depreciation	<u>(142,514)</u>	<u>(94,604)</u>
	<u>\$ 17,205</u>	<u>\$ 65,115</u>

Future minimum lease payments for the above assets under capital leases at September 30, 2012 are as follows:

2012	6,198
2013	8,016
2014	<u>2,988</u>
Total minimum obligations	<u>17,202</u>

**AD ASTRA ROCKET COMPANY
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Interest	<u>537</u>
Present value of net minimum obligations	16,665
Current portion of obligation	<u>(11,755)</u>
Long-term obligation	<u>\$ 4,910</u>

The Company recorded amortization expense related to its capital leases of \$23,955, \$31,941 and \$170,299 for the periods ended September 30, 2012, December 31, 2011, and for the period from inception, July 15, 2005 to September 30, 2012, respectively.

14. Going Concern

As a research and development firm, the Company has not generated significant revenue related to its intended operations since its inception and thereby has experienced recurring net losses and negative cash flows from operations as follows. During the periods ended September 30, 2012, December 31, 2011 and during the period from Inception, July 15, 2005 to September 30, 2012, the Company's net losses were \$2,487,996, \$4,277,425, and \$31,339,917, respectively, and net cash used in operating activities was \$1,743,404, \$2,859,814, and \$21,973,368, respectively. These factors raise a substantial doubt about the Company's ability to continue as a going concern. Historically, the Company has financed its operations using sales of its common and preferred stock and the issuance of convertible debentures to a related party.

The Company received cash from its financing activities for the periods ended September 30, 2012, December 31, 2011 and during the period from Inception, July 15, 2005 to September 30, 2012, of \$1,743,237, \$2,505,263 and \$28,216,051, respectively.

Management plans to continue to focus on raising the funds necessary to fully implement the Company's business plan. The Company's long-term viability depends on its ability to obtain adequate sources of equity or debt funding to meet current commitments and fund the continuation of its business operations and the ability of the Company to ultimately achieve adequate profitability and cash flows from operations to sustain its operations.

15. Contingencies

From time to time, the Company may be involved in various claims and legal actions arising in the ordinary course of business. Management, along with the assistance of counsel, will determine the ultimate disposition and potential impact of these matters on the Company's financial condition, liquidity or results from operations. As of September 30, 2012, there were no pending claims or legal actions in which the Company was involved.