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AMERICAN AMMUNITION INC/FL  
Form 10KSB  
March 31, 2005

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

Form 10-KSB

(Mark One)

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

For the fiscal year ended December 31, 2004

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No.: 000-32379

American Ammunition, Inc.

-----  
(Name of small business registrant in its charter)

California  
-----  
(State or other jurisdiction of  
incorporation or organization)

91-2021594  
-----  
(I.R.S. Employer  
Identification No.)

3545 NW 71st Street  
Miami, FL  
-----  
(Address of principal executive offices)

33147  
-----  
(Zip Code)

Registrant's telephone number: (305) 835-7400

Securities registered under Section 12(b) of the Exchange Act:

Title of each class	Name of each exchange on which registered
None	
-----	-----

Securities registered under Section 12(g) of the Exchange Act:

Common Stock, \$0.001 par value  
-----  
(Title of class)

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Check whether the issuer has (1) filed all reports required to be files by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period the Company was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of Company's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB.

The issuer's revenues for the fiscal year ended December 31, 2004 were \$3,247,368.

The aggregate market value of voting common equity held by non-affiliates as of March 24, 2005 was approximately \$5,271,187.

As of March 24, 2005, there were 75,907,300 shares of Common Stock issued and outstanding.

Transitional Small Business Disclosure Format : Yes  No

### American Ammunition, Inc.

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### Caution Regarding Forward-Looking Information

Certain statements contained in this annual filing, including, without limitation, statements containing the words "believes", "anticipates", "expects" and words of similar import, constitute forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements.

Such factors include, among others, the following: international, national and local general economic and market conditions; demographic changes; the ability of the Company to sustain, manage or forecast its growth; the ability of the Company to successfully make and integrate acquisitions; raw material costs and availability; new product development and introduction; existing government regulations and changes in, or the failure to comply with, government regulations; adverse publicity; competition; the loss of significant customers or suppliers; fluctuations and difficulty in forecasting operating results; changes in business strategy or development plans; business disruptions; the ability to attract and retain qualified personnel; the ability to protect technology; and other factors referenced in this and previous filings.

Given these uncertainties, readers of this Form 10-KSB and investors are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the result of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

### PART I

#### Item 1 - Description of Business

American Ammunition, Inc. (the "Company") was incorporated on February 1, 2000 in accordance with the Laws of the State of California as FirstTelevision.com. It subsequently changed its corporate name to FBI Fresh Burgers International with a business plan of marketing the concept of a national "fast food" restaurant chain to children and young adults, with a menu of fresh burgers, fries and sandwiches.

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This concept was unsuccessful and we had minimal operations until September 2001, when we acquired American Ammunition Inc., a then-privately held Florida corporation. Upon completion of the reverse acquisition transaction with American Ammunition, Inc., we have been engaged in the manufacture and sale of small-arms ammunition for the wholesale and governmental markets.

We are an established small arms munition manufacturer with an existing distribution network. The small-arms ammunition market is principally dominated by three domestic and approximately ten international major manufacturers. Our operations are geared to provide the highest quality product in quantities sufficient to meet our developed wholesale and governmental market demands. We

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are an approved Department of Defense contractor. We began as an assembler and re-loader of ammunition in several calibers. As our operations grew, our management realized that the only way to break into the industry was to become a vertically integrated manufacturer. Our founders invested heavily in research and development, equipment, and technology in prior years to focus on increasing our market share. As a result, we continued manufacturing our initial calibers along with special order ammunition for the Department of Defense. Further streamlining of the operations resulted in the manufacture of the current ammunition product line: 9 millimeter, .45 automatic, .380 automatic, .32 automatic, .40 Smith and Wesson, 38 Special, 30 carbine, 223 Remington, 38 Super, .44 Special, 32 Smith and Wesson Long, 44 special and .44 Magnum. We have also added .44 Magnum, .308, .50 AE and .50 caliber manufactured in Israel and shipped to the Company for distribution under the Company's brand name. We have identified these products as having the largest share of the market for the next several years. We sell our products to both retail consumers and governmental agencies domestically and principally to governmental agencies internationally for military use. During Calendar 2004 and 2003, our sales were approximately 78.06% and 93.77% in domestic markets and approximately 21.94% and 6.23% internationally. We anticipate the international governmental portion of our business to grow in future periods; however, we do not anticipate our international business to outgrow our domestic sales.

Our principal executive offices are located at 3545 NW 71st Street, Miami, Florida 33147 and our telephone number is (305) 835-7400.

### Equipment and Production Line Capabilities

We own all the equipment necessary to take the raw material, consisting primarily of brass, lead, primer and powder, to the finished product, a loaded round of ammunition. The process of manufacturing diverse calibers of ammunition is extremely complex and requires tolerances of +/- .0005" to be maintained throughout the process. Our technology and equipment enable us to produce a large variety of handgun and rifle ammunition. We have a machine shop and maintain our own testing and quality assurance equipment and program. Ammunition is a performance-based product. Therefore, after the manufacturing process is complete, the ammunition must comply with specific protocols such as velocity, accuracy, and pressure. We purchase raw materials in bulk and strive to take advantage of prepayment discounts to produce significant savings in the manufacturing process. There are and have been instances when discounts have been and may be missed due to cash flow restrictions. We continue to evaluate the addition of several products to our existing production lines, including the addition of high speed projectile forming machines to supplement the existing

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casting machines. This addition would effectively double or triple projectile production capacity, while improving projectile quality and performance. We also are making provisions to increase other aspects of production capacity, which would complement long term goals of both production volume and product diversity.

During 2004 and 2003, we acquired equipment which will allowed us to expand our production capacity in areas which they have traditionally been slower than other areas of our manufacturing process. The acquisition of additional presses, for example, has helped us to balance out our assembly line process so that all portions of our projectiles are manufactured in time with each other. We hope this will cut our manufacturing and labor costs and as a result, make us more efficient at producing small arms ammunition.

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During 2004, we acquired laser gauging computer equipment for the purpose of improving and automating quality control processes. This equipment automatically tests and ejects projectiles from the assembly line which do not meet the specified tolerances. We believe that this equipment will assist in the improvement of our products and cut labor costs associated with manual inspection of product.

### Business Strategy

We are an autonomous manufacturer of ammunition, with the technology and equipment to take advantage of the growing small-arms ammunition market. The barrier to entry into the ammunition market is extremely high, however, we are an established small arms munitions manufacturer, with an existing distribution network. We manufacture our ammunition utilizing purchased raw materials to fabricate the necessary components in our own production facility. In management's opinion, the consumer and governmental ammunition market has grown each year and it appears that supply is not keeping up with demand, thus allowing for companies like American Ammunition to make a significant impact in sales through our dealer direct program, established in the first quarter of 2004, and our historically strong relationships with various domestic and foreign governmental agencies.

We continue to seek the necessary working capital to allow us to enlarge our operations to take advantage of our technological capacities, equipment and the existing marketplace.

### Marketing and Sales Distribution

However, in first quarter 2004, we launched our Dealer Direct Program. In doing so, we completely revamped the way we distribute and sell our products domestically. In essence, we eliminated the "middle man" distributor by offering our products directly to and soliciting orders directly from the 66,000 licensed dealers in the United States. In doing this, we may offer our products to dealers cheaper than dealers would otherwise obtain them from distributors, while increasing our profit margins as well. It also eliminates a second freight charge from the distributor to the dealer, as product is shipped directly from our facility to the ultimate seller of our products.

Our marketing strategy consists of several key features to attract dealers directly to our company, rather than to a distributor. First, we are offering

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"net 60" day credit terms to smaller dealers, who would ordinarily be forced to pay for product up front. We have developed a screening process for qualifying these smaller dealers on an individual basis. Although offering net 60 credit terms to dealers results in increased risk to our company in our account receivables as compared to payment in advance, we have exponentially diversified our receivables (and therefore our credit risk) from 13 main distributors to potentially thousands of individual dealers. Secondly, we now offer free freight (shipping) to dealers on certain orders which exceed a specified dollar volume. Shipping of small arms ammunition has always been a large portion of the cost passed to consumers as the product is considered "dense" by shipping companies,

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such as UPS, and requires extra care in shipping. We have determined that we can ship our products at a reduced rate in quantity and can offer free shipping as an incentive on qualified orders. As previously explained, a second freight charge has also been avoided by eliminating the distributor from the transaction. Additionally, our increasing automation and dealer direct program have considerably sped up the time we take to provide a dealer with demanded product. Our management has become aware of an unfulfilled need of dealers to be provided with almost instant gratification when demand at retail establishments increases. Many dealers have communicated with our company complaining that we took their distributors too long to provide them with additional product supply when demand dictated. We believe that our new distribution strategy complimented with recent automation has cut the time it takes a dealer to receive our products by more than half. We only recently upgraded our website to include e-commerce capacity, wherein licensed dealers who are pre-registered with our company can order online direct from us. Sales in this manner have been slow to develop, primarily due to the documentation requirements for pre-qualification of dealers; however, management is hopeful that our dealers will begin to take advantage of the ease of use and time savings related to placing orders directly via electronic means. We anticipate further automation in the way in which our qualified dealers place product orders from our company. We plan to continue to aggressively pursue new customers through promotions, advertising and trade shows. We intend to solicit original equipment manufacturer subcontract work from the three major domestic manufacturers; seek additional means of commercial distribution; seek further Department of Defense and other governmental agency contracts and new relationships; solicit further export sales and, potentially, develop relationships with various mass merchandisers/chain stores.

We have been certified by the United States Small Business Administration as a "qualified HUBZone small business concern." Under this program, small businesses can qualify for special set-aside contracts, get up to a 10% edge in competitive contract bidding or even be the sole-source bidder in some cases. The program's name signifies the effort to promote businesses in "historically underutilized business zones," generally located in "blighted" areas (as defined) and a primary purpose is to create jobs for those who live in such areas. We are marketing our manufacturing flexibility to numerous Department of Defense and commercial munitions manufacturers as subcontractors allowing prime contractors to reap the benefits of our "HUBZone certification", thereby allowing such prime contractors to comply with Federal Acquisition Requirements for the use of "small and under-utilized minority business" in fulfilling government contracts. The Small Business Reauthorization Act of 1997 increased the overall government agencies' procurement goals for small business to 23% and called for HUBZone contracts to increase from 1.5% of these procurements to 3% by 2003.

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### Pricing and Value

We have been able to price our products competitively at a price lower than any of the three major domestic manufacturers: Remington, ATK, and Winchester. We strive to capitalize on the fact that these three competitors have very large corporate infrastructures and, in management's opinion, have to pay much higher labor costs to their manufacturing plant personnel. We believe that our production cost structure and, accordingly, our pricing strategy permits our customers to purchase our product and sell it at a retail price that is lower than competitive distribution channels for our competitors' products.

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### Advertising & Promotion

We intend to gear our advertising towards magazine and print media, focused on the gun and ammunition, handgun and shooting markets. We believe that such advertising will result in greater name recognition among individual consumers. Currently, our sales are generated with very little advertising and we believe that advertising could significantly improve retail/mass merchandiser sales and increase market share.

### Status of Publicly Announced Products and Services Israeli Military Industries Ltd

We have developed a relationship with Israeli Military Industries Ltd. ("IMI"), whereby we work together on individual projects. To date, we have primarily focused their cooperation on federal contracts and on our dealer direct program. In such contracts, projectiles manufactured by IMI have been assembled by our company under IMI's strict quality control requirements. The joint venture has benefitted our company in several ways. First and foremost, IMI has a distinct following as a result of offering very high quality products of the course of many years. Associating our name with IMI's history has added value to our brand and reputation in the small arms ammunition industry. Second, IMI manufactures different calibers and products than us, thereby increasing the catalogue of items we may offer to our dealers. IMI produces commercial ammunition, similar to our company. However, we also specialize in the production of law enforcement and military grade ammunition, which we currently do not have the production capability to produce on our own. Lastly, on past and current cooperation initiatives, IMI has shipped projectiles and materials for future assembly on a consignment basis, thereby saving us the time value of such costs were we to have produced such items or purchased such raw materials ourselves.

### Triton

On February 10, 2004, we executed a non-binding letter of intent to acquire the assets of Triton Ammunition Corporation ("Triton"). This transaction closed on October 19, 2004, with the issuance of 1,111,112 shares of restricted, unregistered common stock valued at \$500,000.

The assets acquired consisted of various pieces of manufacturing machinery, raw materials and finished inventory and various intellectual property rights. Triton conveyed the sole usage patent right agreements and various related licenses for the Hi-Vel and Quik-Shok lines of ammunition.

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The allocation of the purchase price was as follows: Manufacturing equipment - approximately \$134,000; Raw materials and finished inventory - approximately \$89,500; and Patents and a Covenant not-to-compete - approximately \$276,500. As the assigned patents, related licenses and the covenant-not-to-compete have a combined remaining life and/or initial term of approximately 5 years, the Company will amortize the approximate \$276,500 to operations over a 60-month period, commencing on the closing date of the acquisition transaction.

We believe that with the acquisition of certain Triton specialty ammunition and our cooperative relationship with IMI on certain ventures, we allow us to offer an increased product line to our dealers.

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### ECO-AMMOTM

We are now manufacturing and distributing ECO-AMMO(TM). This product utilizes a lead-free projectile with reduced lead pollutants sometimes referred to as "green" ammo. ECO-AMMO(TM) is ideal for indoor ranges since it disintegrates upon impact and, therefore, does not ricochet. We have been acquiring and developing technology to market this environmentally friendly ammunition for some time. The advent of the dealer direct program enables the product to be distributed at a lower cost and should open up the market to more consumers.

### Frangible Aircraft Bullet

We were assigned a serial number (60/325,046) from the U.S. Patent and Trademark Office for our provisional patent application filed on September 26, 2001 for a projectile that will not pierce an aircraft fuselage but will penetrate human soft tissue. The product has been specifically designed for use inside the cabin of a commercial aircraft; however, we have additional applications for use in other environments with similar containment issues, such as security at nuclear power plants, hazardous materials storage facilities, and for consumer home defense. We departed completely from standard ballistics for the design of this projectile to meet what American Ammunition perceives as a growing and unfilled need. Two of the basic design criteria in ballistics are penetration and expansion of the projectile. In this design, these two factors have been controlled to meet the specific requirements of weapons discharged inside a confined space while ensuring the integrity of the surrounding environment. This design is a new concept in close quarter ammunition: a bullet capable of incapacitating an assailant without damaging surrounding structure. Design and material selection allows for the inverted expansion and aft internal collapse of the projectile mass. Our initial testing, using test sections of a commercial airliner fuselage, has revealed that upon impact with the aircraft fuselage, the bullet internally collapses; therefore not allowing for the transfer of kinetic energy forward or penetration above that required for soft tissue penetration. Further, our testing has been successful in ballistic testing using both ordinance gelatin and bovine tissue. This performance criterion is accomplished without sacrificing the standard velocity and accuracy of the caliber being used. A video of those tests can be viewed on our website at [www.a-merc.com](http://www.a-merc.com) in the New Product Section. We believe that these research and development efforts will provide a new product to the public safety and security marketplace.

Industrial Plating Enterprise Company



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Industrial Plating Enterprise Company (IPE), a wholly owned subsidiary of the Company, is a high volume "barrel plating" facility currently operating at below 50.0% of its designed capacity. IPE is meeting all of our projectile plating needs at this time. As our projectile plating requirement grows, IPE has the surplus capacity to increase production to meet that need. IPE's innovative hazardous materials and hazardous waste management and treatment system is fully capable of meeting increased production requirements. IPE's management, intends to explore adding additional metallization and coating processes to diversify its services to the parent company as well as offering its services to other industries with the eventual goal of generating revenue to our company of which there are no guarantees.

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### Competition

The market for small arms ammunition is extremely competitive. Companies such as Remington, Federal and Winchester are all better equipped, more experienced and better financed than us. For years, the large manufacturers have supplied the component parts of the manufacturing process to smaller companies to assemble and distribute. A company making its own components, can produce and market a quality lower cost product. This concept, coupled with technology and progressive and environmentally sound manufacturing practices (i.e. cans and recycled plastic packaging), has resulted in a quality, affordable product reaching the marketplace.

Management undertook a study of the production process and our equipment utilization during December 2004 and the first quarter of 2005. As a result of this study, our management believes that it is feasible to increase our production capacity by 100% to 150% in the immediate future through the renovation and restructuring of our plant flow utilizing our existing equipment and increasing only labor, material and other incidental costs.

### Sources and Availability of Raw Materials

We manufacture our ammunition by creating most of the components ourselves. The materials needed to produce our ammunition products are widely available from numerous third parties. While we believe that no critical shortages of our key raw material components, such as brass, lead and powder. We are cognizant of recent press related to the availability of lead as no new mines have opened in many years due to environmental regulations. We have experienced limited, infrequent delays in receiving lead; however, we have always been able to meet our production requirements from our normal sources. Current demand for our raw material components in the domestic and international markets, principally driven by international military conflicts, may work to our advantage in our contracts and relationships with various domestic and foreign governmental agencies. However, we cannot state with any certainty that any disruption of supply may or may not occur.

### Research and Development

We believe that research and development is an important factor in our future growth. The small arms ammunition industry is closely linked to the latest technological advances. Therefore, we must continually invest in the technology to provide the best quality product to the public and to effectively

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compete with other companies in the industry. No assurance can be made that the Company will have sufficient funds to purchase technological advances as they become available.

### Patents, Copyrights and Trademarks

We intend to protect our original intellectual property with patents, copyrights and/or trademarks as appropriate. Our head stamp "A-MERC " was registered as a trademark on May 10,1994.

We were assigned a serial number (60/325,046) from the U.S. Patent and Trademark Office for our provisional patent application filed on September 26, 2001 for a bullet that will not pierce an aircraft fuselage but will penetrate human soft tissue.

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Our October 2004 acquisition of certain intellectual technology property from Triton Ammunition Corporation included the assignment of the following patents related to the design and manufacture of certain fragmentable projectiles: 4,836,110, dated June 6, 1989; 4,882,822, dated November 28, 1989; and 4,947,755, dated August 8, 1990.

### Governmental Regulation

In accordance with the provisions of Title 1, Gun Control Act of 1968, we are required to be licensed to import firearms and manufacture ammunition for firearms. Such licensing is subject to limitations in Chapter 44, Title 18, United States Code. In the event such licenses are not renewed for any reason, we would have to cease our operations. In accordance with these requirements, we carry two licenses issued by the Department of Treasury, Bureau of Alcohol, Tobacco and Firearms: \* License No. 1-59-025-06-3D 69152 for "06 - Manufacturer of Ammunition for Firearms", which license expires on April 1, 2006; and \* License No. 1-59-025-08-3D-69454 for "08-Importer of Firearm other than Destructive Devices", which license expires on April 1, 2006. We are not aware of any other license requirements or government regulation at a state or federal level specific to their business and believe that we are in full compliance with our existing licenses.

### Effect of Probable Governmental Regulation on the Business

We are not aware of any pending legislation at either the State or Federal level that would change the requirements under which it is licensed and is not aware of any reason why the existing licenses cannot be renewed at their expiration dates. There can be no assurance that legislation will not be proposed and enacted at some time in the future that would preclude us from continuing our operations. Should such legislation be enacted, and should we be precluded from continuing our operations, it would have a materially adverse effect upon our business and future.

### Cost and Effects of Compliance with Environmental Laws

As a manufacturer, we are subject to general Local, State and Federal regulations governing environmental concerns. We believe that we have always been and continue to be in compliance with all such laws. Special precautions have been taken us to ensure that adequate ventilation exists for the portion of

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our operations that utilize lead and/or brass. Additionally, our gunpowder supply is humidity and temperature controlled in a secure and environmentally controlled facility

### Employees

At March 24, 2005, we employ approximately 70 persons. None of our employees are represented by a labor union for purposes of collective bargaining. We consider our relations with our employees to be excellent. We may employ additional personnel, as necessary, to accommodate future sales and production requirements and believe that an ample supply of qualified labor exists in our geographic area to facilitate any required growth.

### Risk Factors

An investment in our common stock has a high degree of risk. Before you invest you should carefully consider the risks and uncertainties described below and the other information in this prospectus. If any of the following risks

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actually occur, our business, operating results and financial condition could be harmed and the value of our stock could go down. This means you could lose all or a part of your investment.

**Risks Relating to Our Business:** We may never become profitable and continue as a going concern because we have had losses since our inception. We may never become profitable and continue as a going concern because we have incurred losses and experienced negative operating cash flow since our formation. We have incurred losses and experienced negative operating cash flow since our formation. For our fiscal years ended December 31, 2004 and 2003, we had a net loss of approximately \$3,361,000 and \$2,968,000, respectively. We may continue to incur significant operating expenses as we maintain our current line of small-arms ammunition and continue research and development toward improving projectile quality and performance. We cannot estimate exactly when our operating expenses will not outpace revenues and result in significant losses in the near term. We may never be able to reduce these losses, which will require us to seek additional debt or equity financing. If such financing is available you may experience significant additional dilution.

There may exist an uncertainty as to our continuation as a going concern: Our audited financial statements for the fiscal years ended December 31, 2004 and 2003 reflect an accumulated deficit of approximately \$19,989,875 and \$16,629,044, since our inception, working capital of approximately \$872,000 and \$2,028,000, and stockholders' equity of approximately \$4,385,000 and \$4,508,000. Our auditor has not issued a going concern opinion on our financial statements; however, our ultimate survivability is dependent upon our being able to generate sufficient cash flows from operations to support its daily operations as well as provide sufficient resources to retire existing liabilities and obligations on a timely basis. Short-term assets and investments income will be sufficient to meet our operating expenses and capital expenditures through 2005. If we continue to incur operating losses, we may not be able to fund continuing business operations, which could lead to the limitation or closure of some or all of our operations.

**We may have to curtail our business if we cannot find adequate funding:** We

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currently have no legally binding commitments with any third parties to obtain any material amount of additional equity or debt financing outside of the financing with La Jolla. We need immediate funds and may not be able to obtain any additional financing in the amounts or at the times that we may require the financing or, if we do obtain any financing, that it would be on acceptable terms because of the following:

- \* we have no assets to pledge as security for the loan; and
- \* we are in poor financial condition where we maybe viewed as a high market risk

As a result, we may not have adequate capital to implement future expansions, maintain our current levels of operation or to pursue strategic acquisitions. Our failure to obtain sufficient additional financing could result in the delay or abandonment of some or all of our development, expansion and expenditures, which could harm our business and the value of our common stock.

Our competitive position may be harmed if we fail to respond to rapid changes in the market for small arms ammunition.

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Our competitive position may be harmed if we fail to respond to rapid changes in the market for small arms ammunition. Our future success will depend significantly on our ability to develop and market new products that keep pace with technological developments and evolving industry standards for hand gun and rifle ammunition. Our delay or failure to develop or acquire technological improvements, adapt our products to technological changes or provide higher quality product lines that appeals to our customers may cause us to lose customers and may prevent us from generating revenue which could ultimately cause us to cease operations.

Our revenues may decrease from production delays due to fire or explosive incidents. Our revenues may decrease from production delays due to fire or explosive incidents. Our ammunition products, involve the manufacture and/or handling of a variety of explosive and flammable materials. This manufacturing and/or handling may result in incidents that will temporarily shut down or otherwise disrupt our manufacturing, causing production delays and resulting in liability for workplace injuries and fatalities. We cannot assure you that we will not experience these types of incidents in the future or that these incidents will not result in production delays, which can lead to a reduction in revenues.

We may incur substantial costs in complying with environmental laws and may be subject to substantial liability resulting from the use of hazardous substances or required cleanup of contaminated sites. Our operations and use of real property are subject to a number of federal, state and local environmental laws and regulations which, among other things, require us to obtain permits to operate and to install pollution control equipment and regulate the generation, storage, handling, transportation, treatment and disposal of hazardous and solid wastes. Our operations, as well as historical operations at our sites, also subject us to liability for the cleanup of releases of hazardous substances. Environmental laws and regulations change frequently, and it is difficult to predict whether and to what extent we may be subject to liability for compliance with environmental laws and regulations.

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Our business operations will be harmed if we are unable to obtain additional funding. Our business operations will be harmed if we are unable to obtain additional funding outside of the La Jolla financing. We believe that our available short-term assets, investment income and financing arrangement with La Jolla will be sufficient to meet our operating expenses and capital expenditures through the end of fiscal year 2005. We do not know if additional financing will be available when needed, or if it is available, if it will be available on acceptable terms. Insufficient funds may prevent us from implementing our business strategy or may require us to delay, scale back or eliminate certain contracts for the provision of our technology and products.

Our competitors may misappropriate our intellectual property because we have only one trademark and five patents.

We attempt to protect our limited proprietary property through trademark, trade secret, nondisclosure and confidentiality measures. Such protections, however, may not preclude competitors from developing similar technologies. Any inability to adequately protect our proprietary technology could harm our ability to compete.

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Our future success and ability to compete depends in part upon our proprietary technology and our trademark, which we attempt to protect with a combination of trademark and confidentiality procedures and contractual provisions. These legal protections afford only limited protection and are time-consuming and expensive to obtain and/or maintain. Further, despite our efforts, we may be unable to prevent third parties from infringing upon or misappropriating our intellectual property.

Risks Relating to Our Current Financing Arrangement: There are a large number of shares underlying our convertible debentures and warrants that may be available for future sale and the sale of these shares may depress the market price of our common stock.

As of January 5, 2005, we had 74,740,580 shares of common stock issued and outstanding and convertible debentures outstanding that may be converted into an estimated 21,430,661 shares of common stock at current market prices, and outstanding warrants to purchase 2,666,350 shares of common stock. In addition, the number of shares of common stock issuable upon conversion of the outstanding convertible debentures may increase if the market price of our stock declines. All of the shares, including all of the shares issuable upon conversion of the debentures and upon exercise of our warrants, may be sold without restriction. The sale of these shares may adversely affect the market price of our common stock.

The continuously adjustable conversion price feature of our convertible debentures could require us to issue a substantially greater number of shares, which will cause dilution to our existing stockholders.

Our obligation to issue shares upon conversion of our convertible debentures is essentially limitless. The following is an example of the amount of shares of our common stock that are issuable, upon conversion of our convertible debentures (excluding accrued interest), based on market prices 25%, 50% and 75% below the market price, as of January 5, 2005 of \$0.16.

Number	% of
--------	------

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%Below Market -----	Price Per Share -----	With Discount at 24% -----	of Shares Issuable -----	Outstanding Stock -----
25%	\$.12	\$.0912	29,462,048	28.27%
50%	\$.08	\$.0608	45,524,822	37.85%
75%	\$.04	\$.0304	93,713,145	55.63%

As illustrated, the number of shares of common stock issuable upon conversion of our convertible debentures will increase if the market price of our stock declines, which will cause dilution to our existing stockholders.

The continuously adjustable conversion price feature of our convertible debentures may encourage investors to make short sales in our common stock, which could have a depressive effect on the price of our common stock.

The convertible debentures are convertible into shares of our common stock at a 24% discount to the trading price of the common stock prior to the conversion. The significant downward pressure on the price of the common stock as the selling stockholder converts and sells material amounts of common stock

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could encourage short sales by investors. This could place further downward pressure on the price of the common stock. The selling stockholder could sell common stock into the market in anticipation of covering the short sale by converting their securities, which could cause the further downward pressure on the stock price. In addition, not only the sale of shares issued upon conversion or exercise of debentures, warrants and options, but also the mere perception that these sales could occur, may adversely affect the market price of the common stock.

The issuance of shares upon conversion of the convertible debentures and exercise of outstanding warrants may cause immediate and substantial dilution to our existing stockholders.

The issuance of shares upon conversion of the convertible debentures and exercise of warrants may result in substantial dilution to the interests of other stockholders since the selling stockholders may ultimately convert and sell the full amount issuable on conversion. Although the selling stockholders may not convert their convertible debentures and/or exercise their warrants if such conversion or exercise would cause them to own more than 9.9% of our outstanding common stock, this restriction does not prevent the selling stockholders from converting and/or exercising some of their holdings and then converting the rest of their holdings. In this way, the selling stockholders could sell more than this limit while never holding more than this limit. There is no upper limit on the number of shares that may be issued which will have the effect of further diluting the proportionate equity interest and voting power of holders of our common stock, including investors in this offering.

In The Event That Our Stock Price Declines, The Shares Of Common Stock Allocated For Conversion Of The Convertible Debentures and Registered Pursuant To Our Pending Prospectus May Not Be Adequate And We May Be Required to File A Subsequent Registration Statement Covering Additional Shares. If The Shares We Have Allocated And Are Registering Herewith Are Not Adequate And We Are Required To File An Additional Registration Statement, We May Incur Substantial Costs In

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Connection Therewith.

Based on our current market price and the potential decrease in our market price as a result of the issuance of shares upon conversion of the convertible debentures, we have made a good faith estimate as to the amount of shares of common stock that we are required to register and allocate for conversion of the convertible debentures. We have allocated and registered 42,861,322 shares to cover the conversion of the convertible debentures. In the event that our stock price decreases, the shares of common stock we have allocated for conversion of the convertible debentures and are registering hereunder may not be adequate. If the shares we have allocated to the registration statement are not adequate and we are required to file an additional registration statement, we may incur substantial costs in connection with the preparation and filing of such registration statement.

If We Are Required for any Reason to Repay Our Outstanding Convertible Debentures, We Would Be Required to Deplete Our Working Capital, If Available, Or Raise Additional Funds. Our Failure to Repay the Convertible Debentures, If Required, Could Result in Legal Action Against Us, Which Could Require the Sale of Substantial Assets.

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We entered into a Securities Purchase Agreement with La Jolla on October 4, 2002 for the sale of (i) \$250,000 in convertible debentures and (ii) warrants to buy 30,000,000 shares of our common stock. On March 13, 2003 and May 6, 2003, La Jolla advanced an aggregate of \$350,000 to our company which such funding was allocated towards the principal balance of our convertible debentures. As of January 5, 2005, \$266,350 of the debenture remained outstanding. The convertible debentures are due and payable, with 8% interest on June 30, 2006, unless sooner converted into shares of our common stock. In addition, any event of default could require the early repayment of the convertible debentures at a price equal to 125% of the amount due under the debentures. We anticipate that the full amount of the convertible debentures, together with accrued interest, will be converted into shares of our common stock, in accordance with the terms of the convertible debentures. If we are required to repay the convertible debentures, we would be required to use our limited working capital and raise additional funds. If we were unable to repay the debentures when required, the debenture holders could commence legal action against us and foreclose on all of our assets to recover the amounts due. Any such action would require us to curtail or cease operations.

Risks Relating to Our Common Stock: If We Fail to Remain Current on Our Reporting Requirements, We Could be Removed From the OTC Bulletin Board Which Would Limit the Ability of Broker-Dealers to Sell Our Securities and the Ability of Stockholders to Sell Their Securities in the Secondary Market.

Companies trading on the OTC Bulletin Board, such as us, must be reporting issuers under Section 12 of the Securities Exchange Act of 1934, as amended, and must be current in their reports under Section 13, in order to maintain price quotation privileges on the OTC Bulletin Board. If we fail to remain current on our reporting requirements, we could be removed from the OTC Bulletin Board. As a result, the market liquidity for our securities could be severely adversely affected by limiting the ability of broker-dealers to sell our securities and the ability of stockholders to sell their securities in the secondary market.

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Our directors and executive officers beneficially own approximately 36.46% of our stock; their interests could conflict with yours; significant sales of stock held by them could have a negative effect on our stock price; stockholders may be unable to exercise control.

As of January 5, 2005, our executive officers and directors, which primarily includes the Fernandez family, beneficially own approximately 36.46% of our common stock. As a result, our executive officers and directors will have significant influence to:

- \* elect or defeat the election of our directors;
- \* amend or prevent amendment of our articles of incorporation or bylaws;
- \* effect or prevent a merger, sale of assets or other corporate transaction; and
- \* control the outcome of any other matter submitted to the stockholders for vote.

As a result of their ownership and positions, our directors and executive officers collectively are able to significantly influence all matters requiring stockholder approval, including the election of directors and approval of

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significant corporate transactions. In addition, sales of significant amounts of shares held by our directors and executive officers, or the prospect of these sales, could adversely affect the market price of our common stock. Management's stock ownership may discourage a potential acquirer from making a tender offer or otherwise attempting to obtain control of us, which in turn could reduce our stock price or prevent our stockholders from realizing a premium over our stock price.

Our Common Stock is Subject to the "Penny Stock" Rules of the SEC and the Trading Market in Our Securities is Limited, Which Makes Transactions in Our Stock Cumbersome and May Reduce the Value of an Investment in Our Stock.

The Securities and Exchange Commission has adopted Rule 15c-9 which establishes the definition of a "penny stock," for the purposes relevant to us, as any equity security that has a market price of less than \$5.00 per share or with an exercise price of less than \$5.00 per share, subject to certain exceptions. For any transaction involving a penny stock, unless exempt, the rules require:

- \* that a broker or dealer approve a person's account for transactions in penny stocks; and
- \* the broker or dealer receive from the investor a written agreement to the transaction, setting forth the identity and quantity of the penny stock to be purchased

In order to approve a person's account for transactions in penny stocks, the broker or dealer must:

- \* obtain financial information and investment experience objectives of the person; and
- \* make a reasonable determination that the transactions in penny stocks are suitable for that person and the person has sufficient knowledge and experience in financial matters to be capable of evaluating the risks of transactions in penny stocks.



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The broker or dealer must also deliver, prior to any transaction in a penny stock, a disclosure schedule prescribed by the Commission relating to the penny stock market, which, in highlight form:

- \* sets forth the basis on which the broker or dealer made the suitability determination; and
- \* that the broker or dealer received a signed, written agreement from the investor prior to the transaction.

Generally, brokers may be less willing to execute transactions in securities subject to the "penny stock" rules. This may make it more difficult for investors to dispose of our common stock and cause a decline in the market value of our stock.

Disclosure also has to be made about the risks of investing in penny stocks in both public offerings and in secondary trading and about the commissions payable to both the broker-dealer and the registered representative, current quotations for the securities and the rights and remedies available to an investor in cases of fraud in penny stock transactions. Finally, monthly statements have to be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks.

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### Item 2 - Description of Property

We lease our corporate office and manufacturing facility from our controlling stockholder under a long-term operating lease agreement. The lease requires a monthly payment of approximately \$5,735, including applicable State sales taxes. We are responsible for all utilities and maintenance expenses. The lease expires on December 1, 2009 and contains a clause that upon expiration, the Company and the controlling shareholder shall renegotiate the annual rental amount.

Our subsidiary, IPE, leases its manufacturing facility from an unrelated third-party under a long-term operating lease agreement. This lease is for a period of five (5) years and requires graduated monthly payments, changing on the lease anniversary date, ranging from approximately \$1,751 to \$1,914, plus the applicable sales taxes. The Company is responsible for all utilities and maintenance expenses. The lease expires on February 28, 2007 and may be renewed for an additional five (5) year term at a rental rate of approximately \$1,971, plus applicable sales taxes for the first renewal year and 3.0% increase on each succeeding anniversary date. Total rent expense under this lease was approximately \$20,752 and \$16,622, respectively, for each of the years ended December 31, 2004 and 2003.

In May 2004, we entered into a long-term lease agreement for a warehouse facility in close proximity to our primary office and manufacturing facility with an unrelated third-party. This lease is for a period of two (2) years and requires payments of approximately \$6,206 per month for the first 12 months and approximately \$6,393 for the second 12 months, plus applicable sales taxes. We are responsible for all utilities and maintenance expenses. This lease expires on May 31, 2006. Further, we are responsible for any incremental real estate taxes and property insurance in excess of the amounts incurred by the landlord for the calendar year immediately preceding the execution of the lease.

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Future minimum rental payments on the above leases are as follows:

Year ended December 31,	Amount
2005	\$ 166,974
2006	117,244
2007	72,643
2008	68,815
2007	68,815
Totals	\$ 494,491
	=====

For the respective years ended December 31, 2004 and 2003, the Company paid an aggregate of \$131,804 and \$87,826 for rent under these agreements.

### Item 3 - Legal Proceedings

The Company is not a party to any pending legal proceedings, and no such proceedings are known to be contemplated.

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### Item 4 - Submission of Matters to a Vote of Security Holders

The Company has not conducted any meetings of shareholders during the preceding quarter or periods subsequent thereto.

## PART II

### Item 5 - Market for Company's Common Stock and Related Stockholder Matters

#### Market for Trading

Our common stock of the Company currently is quoted on the NASDAQ Over the Counter Bulletin Board under the symbol "AAMI" and has been since October 23, 2001. Prior to that time, our common stock was approved for trading under symbol "FBIB," although it never traded under that symbol. The ask/high and bid/low information for each quarter since October 23, 2001 are as follows:

Quarter	Ask/High	Bid/Low
1/1/2002 - 3/31/2002	0.81	0.33
4/1/2002 - 6/30/2002	0.65	0.36
7/1/2002 - 9/30/2002	0.57	0.31
10/1/2002 - 12/31/2002	0.47	0.38
1/1/2003 - 3/31/2003	0.78	0.53
4/1/2003 - 6/30/2003	0.85	0.42
7/1/2003 - 9/30/2003	0.55	0.37
10/1/2003 - 12/31/2003	0.42	0.22

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1/1/2004 - 3/31/2004	0.50	0.27
4/1/2004 - 6/30/2004	0.42	0.17
7/1/2004 - 9/30/2004	0.27	0.17
10/1/2004 - 12/31/2004	0.24	0.15
1/1/2005 - 3/20/2005	0.17	0.09

Please note that over-the-counter market quotations have been provided herein. The quotations reflect inter-dealer prices, without retail markup, mark-down or commission and may not represent actual transactions.

As of December 31, 2004, we had approximately 178 shareholders of record, exclusive of our stockholders with their holdings in street name.

### Common Stock

The holders of the issued and outstanding shares of common stock are entitled to receive dividends when, as and if declared by our Board of Directors out of any funds lawfully available therefore. The Board of Directors intends to retain future earnings to finance the development and expansion of our business and does not expect to declare any dividends in the foreseeable future. The

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holders of the common stock have the right, in the event of liquidation, to receive pro rata all assets remaining after payment of debts and expenses. The common stock does not have any preemptive rights and does not have cumulative voting rights. The issued and outstanding shares of common stock are fully paid and nonassessable. Holders of shares of common stock are entitled to vote at all meetings of such shareholders for the election of directors and for other purposes. Such holders have one vote for each share of common stock held by them.

### Transfer Agent

Our independent stock transfer agent for our common and preferred stock is Atlas Stock Transfer Corporation. Their mailing address and telephone number is 5899 South State Street, Salt Lake City, Utah 84107; (801) 266-7151.

### Reports to Stockholders

The Company plans to furnish its stockholders with an annual report for each fiscal year ending December 31 containing financial statements audited by its registered independent public accounting firm. In the event the Company enters into a business combination with another Company, it is the present intention of management to continue furnishing annual reports to stockholders. Additionally, the Company may, in its sole discretion, issue unaudited quarterly or other interim reports to its stockholders when it deems appropriate. The Company intends to maintain compliance with the periodic reporting requirements of the Securities Exchange Act of 1934.

### Dividend policy

No dividends have been paid to date and the Company's Board of Directors does not anticipate paying dividends in the foreseeable future. It is the current policy to retain all earnings, if any, to support future growth and expansion.

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### Item 6 - Management's Discussion and Analysis or Plan of Operation

#### Caution Regarding Forward-Looking Information

Certain statements contained in this annual filing, including, without limitation, statements containing the words "believes", "anticipates", "expects" and words of similar import, constitute forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements.

Such factors include, among others, the following: international, national and local general economic and market conditions; demographic changes; the ability of the Company to sustain, manage or forecast its growth; the ability of the Company to successfully make and integrate acquisitions; raw material costs and availability; new product development and introduction; existing government regulations and changes in, or the failure to comply with, government regulations; adverse publicity; competition; the loss of significant customers

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or suppliers; fluctuations and difficulty in forecasting operating results; changes in business strategy or development plans; business disruptions; the ability to attract and retain qualified personnel; the ability to protect technology; and other factors referenced in this and previous filings.

Given these uncertainties, readers of this Form 10-KSB and investors are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the result of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

#### General

American Ammunition, Inc. is a holding company with two operating subsidiaries: F&F Equipment, Inc. and Industrial Plating Enterprise Co.

F&F Equipment, Inc. (F&F) was incorporated on October 4, 1983 under the laws of the State of Florida. F&F was formed to engage principally in the "import, export, retail & wholesale of firearms equipment, ammunition & other devices and for the purpose of transacting any and/or all lawful business." F&F conducts its business operations under the assumed name of "American Ammunition."

In June 2002, American Ammunition, Inc. formed a wholly owned subsidiary, Industrial Plating Enterprise Co. (IPE), which started production on June 14, 2002. IPE is a fully licensed and approved electrochemical metallization facility with significant capacity for processing our line of projectiles as well as other products and services while employing environmentally sound water conservation and proven waste treatment techniques.

#### Results of Operations

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Year ended December 31, 2004 compared to Year ended December 31, 2003

During the year ended December 31, 2004, we experienced aggregate net revenues of approximately \$3,247,000, with approximately \$1,535,000 being realized during the 4th quarter, as compared to approximately \$1,985,000 in total net revenues for the year ended December 31, 2003.

We experienced costs of goods sold of approximately \$4,621,000 for the year ended December 31, 2003 as compared to approximately \$3,232,000 for the year ended December 31, 2003.

During 2004 and 2003, we experienced negative trends off of our standard production costs for material and labor due to difficulties in training new employees, adding new products to our catalog and lower than expected orders during the first two quarters of 2004 due to uncontrollable delays in ordering by various U. S. Governmental entities. Management is of the opinion that the production labor force is stable and able to maintain a constant standard of quality for future periods. We experience variable costs in the area of material consumption and direct labor. We have recognized depreciation expense on production equipment of approximately \$729,000 and \$669,000, respectively, in the above cost of goods expense totals. These depreciation levels are anticipated to fluctuate nominally in future periods based upon either the full depreciation of older equipment and/or the addition of new equipment to expand

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capacity. For the year ended December 31, 2004 and 2003, respectively, we generated a negative gross profit of approximately \$(1,373,298), or (42.29%), and approximately \$(1,247,000), or (62.82%). Based on orders received and products shipped during the first quarter of 2005 (through the filing date of this document) and our ongoing conversations with various customers that we should be able to generate a positive gross profit in future periods..

We experienced nominal research and development expenses of approximately \$11,000 and \$4,000, respectively, during the years ended December 31, 2004 and 2003, principally related to the expansion of our product line.

Other general and administrative expenses increased by approximately \$440,000 from approximately \$1,127,000 for the year ended December 31, 2003 as compared to approximately \$1,567,000 for the year ended December 31, 2004. The most significant increases relate to advertising and marketing expenses (approximately \$324,000), office and administrative wages and salaries and overall office overhead (approximately \$116,000).

During 2004 and 2003, respectively, we experienced charges to operations of approximately \$382,000 and \$883,000 for compensation expense related to common stock issuances at less than "fair value". The calculation of these charges result from our issuing common stock for either cash or services at valuations below the closing quoted market price of our common stock (as discounted, as applicable) and either the cash received or the value of the services provided to us by third parties. During 2003, we experienced a charge of approximately \$94,000 for the amortization of the Beneficial Conversion Feature Discount on our Preferred Stock. This charge results from the difference between the closing quoted market price on our common stock and the equivalent converted price of our Mandatory Convertible Preferred Stock which was sold and converted during 2003.

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We recognized a net loss of approximately \$(3,318,000) and \$(2,968,000) for the respective years ended December 31, 2004 and 2003, respectively, or \$(0.05) and \$(0.05) per share.

Year ended December 31, 2003 compared to Year ended December 31, 2002

During the year ended December 31, 2003, we experienced aggregate net revenues of approximately \$1,985,000, with approximately \$769,000 being realized during the 4th quarter, as compared to approximately \$1,409,000 for the year ended December 31, 2002.

We experienced costs of goods sold of approximately \$3,232,000 for the year ended December 31, 2003 as compared to approximately \$2,457,000 for the year ended December 31, 2002. During 2003, we experienced negative trends off of our standard production costs for material and labor due to difficulties in training new employees and adding new products to our catalog. Management is of the opinion that the production labor force is stable and able to maintain a constant standard of quality for future periods. We experience variable costs in the area of material consumption and direct labor. We have recognized depreciation expense on production equipment of approximately \$669,000 and \$653,000, respectively, in the above cost of goods expense totals. These

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depreciation levels are anticipated to remain fairly constant for future periods as management does not anticipate any significant capital equipment acquisitions in future periods. Further, the addition of the Industrial Plating Enterprise Co. equipment allows us to produce certain components which were previously outsourced to unrelated third parties. For the year ended December 31, 2003 and 2002, respectively, we have generated a negative gross profit of approximately \$(1,247,000), or (62.82%), and approximately \$(1,047,000), or (74.31%). We anticipated that with the fulfillment of the various private labeling agreements and government contracts, continued retail consumer demand for our product line, lower production costs being experienced from internally generated plating activities and adequate liquidity, we would be able to generate a positive gross profit in future periods. Further, based on production cost information developed during the 4th quarter of 2002 and further refined during 2003, management has developed a new model for the pricing of its products to its customers. It is anticipated that this model will allow management to better manage expense levels, control labor costs and maximize revenue opportunities.

We experienced nominal research and development expenses of approximately \$4,000 and \$3,700, respectively, during the years ended December 31, 2003 and 2002, principally related to the expansion of our product line.

Other general and administrative expenses increased by approximately \$282,000 from approximately \$845,000 for the year ended December 31, 2002 as compared to approximately \$1,127,000 for the year ended December 31, 2003. The most significant increases relate to advertising and marketing expenses, office and administrative wages and salaries and overall office overhead.

During 2003 and 2002, respectively, we experienced charges to operations of approximately \$883,000 and \$11,500 for compensation expense related to common stock issuances at less than "fair value". The calculation of these charges result from our issuing common stock for either cash or services at valuations below the closing quoted market price of our common stock (as discounted, as

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applicable) and either the cash received or the value of the services provided to us by third parties. During 2003, we experienced a charge of approximately \$94,000 for the amortization of the Beneficial Conversion Feature Discount on our Preferred Stock. This charge results from the difference between the closing quoted market price on our common stock and the equivalent converted price of our Mandatory Convertible Preferred Stock which was sold and converted during 2003.

We recognized a net loss of approximately \$(2,968,000) and \$(1,883,000) for the respective years ended December 31, 2003 and 2002, respectively, or \$(0.05) and \$(0.04) per share.

### Liquidity

As of December 31, 2004 and 2003, respectively, we had working capital of approximately \$872,000 and \$2,000,000. Our working capital position improved significantly at December 31, 2003 due to the volume of shipments during the 4th quarter to our customers and increases in inventory to support the pending U. S. Government contracts. At December 31, 2004, our working capital declined due to liabilities for customer deposits received at year-end for orders which had not been produced and shipped; but, were completed during the quarter ended March 31, 2005 and increased trade account payable levels for 4th quarter 2004 production on orders which were shipped under our "net 60" terms programs related to our dealer direct sales efforts.

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We have used cash in operating activities of approximately \$(649,000) and \$(2,918,000) during the years ended December 31, 2004 and 2003, respectively.

### Capital Requirements

During the years ended December 31, 2004 and 2003, respectively, we added approximately \$717,000 and \$289,000 in new equipment. The equipment added in 2004 was related to 1) the expansion of our production line; 2) the addition of computerized quality control inspection processes and 3) the automation of our packaging line.

Depending on future demand for our products, we may need to further increase our production capability and management is of the opinion that adequate equipment, either new or used, will be available to facilitate any future expansion.

### Convertible Debenture

The Company entered into a Securities Purchase Agreement with La Jolla Cove Investors, Inc. ("La Jolla") on October 4, 2002 for the sale of (i) \$250,000 in convertible debentures and (ii) warrants to buy 30,000,000 shares of our common stock. On March 13, 2003 and May 6, 2003, La Jolla advanced an aggregate of \$350,000 to our company which such funding was allocated towards the principal balance of our convertible debentures.

As of December 31, 2004, the outstanding balance on the convertible debenture is approximately \$266,365 and we have approximately 2,663,650 warrants outstanding.

The debentures bear interest at 8%, mature on June 30, 2006, and are

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convertible into our common stock, at the selling stockholder's option. The convertible debentures are convertible into the number of our shares of common stock equal to the principal amount of the debentures being converted multiplied by 11, less the product of the conversion price multiplied by 10 times the dollar amount of the debenture. The conversion price for the convertible debentures is the lesser of (I) \$1.00 or (ii) seventy six percent of the average of the five lowest volume weighted average prices during the twenty (20) trading days prior to the conversion. Accordingly, there is in fact no limit on the number of shares into which the debenture may be converted. However, in the event that our market price is less than \$.30, we will have the option to prepay the debenture at 125% rather than have the debenture converted. In addition, the selling stockholder is obligated to exercise the warrant concurrently with the submission of a conversion notice by the selling stockholder. As of December 31, 2004, the warrant is exercisable into 2,663,650 shares of common stock at an exercise price of \$1.00 per share.

In December 2004, we entered into an addendum to the convertible debenture and warrant whereby the Company agreed to the following:

- \* the discount multiplier was reduced from eighty percent to seventy six percent;
- \* within five business days after this registration statement being declared effective, La Jolla is required to submit a debenture conversion in the amount of \$10,000 and every ten business days thereafter La Jolla shall submit three additional debenture conversion in the amount of \$10,000 each;

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- \* within five business days after this registration statement being declared effective, La Jolla shall wire \$400,000 to us as a prepayment towards the exercise of its warrant; and
- \* immediately following the sale of all shares held by La Jolla in connection with the debenture conversions in the aggregate amount of \$40,000, La Jolla shall wire \$275,000 to us as a prepayment towards the exercise of its warrant and shall submit a debenture conversion in the amount of \$6,250 on the first business day of each month until the debenture is no longer outstanding.

LaJolla has contractually agreed to restrict its ability to convert or exercise its warrants and receive shares of our common stock such that the number of shares of common stock held by them and their affiliates after such conversion or exercise does exceed 4.9% of the then issued and outstanding shares of common stock.

Due to the contractually agreed mandatory conversion of this Debenture, the Company has reflected this transaction in its balance sheet as a "mezzanine" level debt obligation on its balance sheet, between "Total Liabilities" and "Stockholders' Equity". Upon the respective mandatory conversion, the Company will relieve the respective portion of the Debenture and the any related accrued, but unpaid interest, and credit this amount to the respective "common stock" and "additional paid-in capital" accounts in the stockholder's equity section for the par value and excess amount over the par value of the respective shares issued.

As the warrant is non-detachable from the Debenture and requires



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simultaneous exercise upon conversion of the Debenture, no value was assigned to the issued warrant. Upon exercise of the warrant, the Company will record the issuance of the underlying shares as a new issuance of common stock on the date of each respective exercise.

On various dates through December 31, 2003, the Debenture Holder elected to convert an aggregate \$208,635, through 24 separate transactions, in outstanding Debenture principal into restricted, unregistered common stock. This election caused the Company to issue 4,561,753 shares of restricted, unregistered common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 2,086,350 shares of the Company's restricted, unregistered common stock for gross proceeds of \$2,086,350.

On various dates between January 1, 2004 and December 31, 2004, the Debenture Holder elected to convert an aggregate \$150,000, through 6 separate transactions, in outstanding Debenture principal into registered common stock. This election caused the Company to issue 4,900,000 shares of common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 1,500,000 shares of the Company's common stock for gross proceeds of \$1,500,000.

### Item 7 - Index to Financial Statements

The required financial statements begin on page F-1 of this document.

### Item 8 - Changes in and Disagreements with Accountants on Accounting and Financial Disclosures

None

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### Item 8A - Controls and Procedures

As of the date of this filing, an evaluation of the effectiveness of the design and operation of American Ammunition, Inc.'s disclosure controls and procedures was carried out under the supervision and with the participation of management, including our Chief Executive and Financial Officer. Based upon that evaluation, our Chief Executive and Financial Officer concluded that the Company's disclosure controls and procedures are effective. There have been no significant changes in our internal controls or in other factors that could significantly affect internal controls subsequent to the date we carried out the evaluation.

## PART III

### Item 9 - Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(a) of the Exchange Act

The directors and executive officers serving the Company are as follows:

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Name	Age	Position Held and Tenure
J.A. Fernandez, Sr.	67	Chairman of the Board and Director of Sales
Andres F. Fernandez	38	President and Chief Executive Officer
Emilio D. Jara	39	Vice-President of Operations, Secretary and Director
Maria A. Fernandez	44	Director

All directors hold office until the next annual meeting of the Company's shareholders and until their successors have been elected and qualify. Officers serve at the pleasure of the Board of Directors. The officers and directors will devote such time and effort to the business and affairs of the Company as may be necessary to perform their responsibilities as executive officers and/or directors of the Company.

### Family Relationships

J.A. Fernandez, Sr. is the father of Andres and Maria Fernandez. There are no other family relationships between or among the executive officers and directors of our company.

### Business Experience

J. A. Fernandez, Sr., age 67, currently serves as the Chairman of the Board and Director of Sales. He has been employed by us since our inception in 1983. Mr. Fernandez is the founder F&F Equipment, which began as a family business, and is responsible for our sales activities. Mr. Fernandez has over 40 years experience in diverse industries including aerospace, advanced polymer manufacturing, munitions, mining and processing of gemstones and metal ores and has utilized such experience for the growth and development of the Company. He is fluent in Spanish.

Andres Fernandez, age 38, currently serves as President and Chief Executive Officer. Mr. Fernandez has served in each of these capacities since September 2001. He has been employed by our company for over a decade. Mr. Fernandez is responsible for day to day operations and has been a driving force behind our

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company and our success in becoming a vertically integrated manufacturer. He studied physics and calculus at St. Thomas University, FL and at the University of Miami, FL. He is a licensed pilot, having graduated from the American Institute of Aeronautics, FL, and received his certificate as a private pilot (fixed wing) as well as private helicopter (rotary) in 1989. In 1989, Mr. Fernandez graduated from the Institute of Public Service (Pan Am), GA as a tactical rappel instructor. In 1990, he graduated from Omni Explosives, TN with a specialty in tactical explosives. Mr. Fernandez was certified by the Florida Department of Law Enforcement Academy in special operations/entry techniques in 1990. He has served as a tactical advisor to U.S. Treasury Department, Bureau of Alcohol, Tobacco and Firearms, U.S. Customs Service and the Florida Department of Law Enforcement. He has received numerous commendations and letters of appreciation. He also served on the Board of Veterans Affairs (Hialeah, FL) from 1990 to 1991. He is fluent in Spanish.

Emilio Jara, age 39, currently serves as Vice President of Operations, Secretary and a Director. Mr. Jara has served in each of these capacities since September 2001. He has been employed with our company since 1988. He has been an

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integral part of our technological growth. His abilities have contributed to our research and development and subsequent increase in the number of production lines. Mr. Jara is extremely well versed in metallurgical and ballistic issues. He studied business administration at Miami- Dade Community College (1984/1985). In 1989, he graduated from the Institute of Public Service (Pan Am), GA as a Tactical Rappel Instructor. In 1990, Mr. Jara graduated from Omni Explosives, TN with a specialty in Tactical Explosives. He is fluent in Spanish.

Maria A. Fernandez, age 44, currently serves as a Director. Mrs. Fernandez has served as a Director since September 2001. She has been the managing partner at Fernandez Friedman Grossman & Kohn PLLC, a Louisville, KY law firm, since May 1998. Prior to that date, she was a partner at Taustine Post Sotsky Berman Fineman & Kohn. She concentrates her legal practice in the areas of estate planning, probate and administration. She also practices in the areas of Medicaid and disability planning, corporate and individual taxation and corporate law, with an emphasis in closely held corporations. She is a graduate of the University of Miami, FL (Bachelor of Business Administration and Master of Professional Accounting) and the Brandeis School of Law at the University of Louisville, KY. Ms. Fernandez is licensed to practice in Kentucky and Florida. She has lectured in the areas of estate planning and probate, Medicaid planning and elder law. She is a member of the Louisville, Florida, Kentucky and American Bar Associations and is fluent in Spanish. Ms. Fernandez is the past President of the Women Lawyers Association of Jefferson County, Kentucky and current Board Member of the Louisville Bar Association. A Graduate of the Kentucky Women's Leadership Network, she is active in various civic organizations and is on the board of several non-profit corporations.

### Compliance with Section 16(a) of the Securities Exchange Act

Section 16(a) of the Securities Exchange Act of 1934 requires our directors, certain officers and persons holding 10% or more of our common stock to file reports regarding their ownership and regarding their acquisitions and dispositions of the Registrant's common stock with the Securities and Exchange Commission ("SEC"). Such persons are required by SEC regulations to furnish our company with copies of all Section 16(a) forms they file. Based solely upon a review of Forms 3 and 4 and amendments thereto furnished to us under Rule 16a-3(d) during fiscal 2003, and certain written representations from executive officers and directors, we are unaware that any required reports that have not been timely filed.

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### Code of Ethics

We have not adopted a code of ethics that applies to our principal executive officer, principal financial officer, principal accounting officer or controller, or persons performing similar functions. We have not adopted such a code of ethics because all of management's efforts have been directed to building the business of the company; at a later time, such a code of ethics may be adopted by the Board of Directors.

### Committees of the Board of Directors

We presently do not have an audit committee, compensation committee, nominating committee, an executive committee of our board of directors, stock plan committee or any other committees. However, our board of directors will establish various committees during the current fiscal year.

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### Terms of Office

Our directors are appointed for a one year term to hold office until the next annual general meeting of the holders of our Common Stock or until removed from office in accordance with our By-Laws. Our officers are appointed by our Board of Directors and hold office until removed by our Board of Directors.

### Conflicts of Interest

We know of no identified or disclosed conflicts of interest among our officers or directors and the affairs of the Company.

### Indemnification for Securities Act Liabilities

The California Corporations Code provides for the indemnification of directors, officers, employees and agents under the circumstances as set forth in Section 317 thereof. Section 317 permits a corporation to indemnify its agents, typically directors and officers, for expenses incurred or settlements or judgments paid in connection with certain legal proceedings. Only those legal proceedings arising out of such persons' actions as agents of the corporation may be grounds for indemnification.

Whether indemnification may be paid in a particular case depends on whether the agent wins, loses or settles the suit and upon whether a third party or the corporation itself is the plaintiff. Section 317 provides for mandatory indemnification, no matter who the plaintiff is, when an agent is successful on the merits of a suit. In all other cases, indemnification is permissive and sometimes requires approval of the court in which the suit is or was pending.

If the agent loses or settles a suit with a plaintiff other than the Company or someone who did not threaten or bring suit on our behalf, the agent may be indemnified for expenses incurred and settlements or judgments paid. That indemnification may be authorized upon a finding that the agent acted in good faith and in a manner he or she reasonably believed to be in our best interests,

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and, in a criminal proceeding, only where the agent had no reasonable cause to believe his or her conduct was unlawful. If the agent loses or settles a suit with us or a plaintiff who threatened or brought suit on our behalf, the agent may be indemnified for expenses actually and reasonably incurred in connection with the defense or settlement of the action. Such indemnification may be authorized upon a finding that the agent acted in good faith and in a manner he or she believed to be in our best interests and the best interests of our shareholders. No indemnification is permitted where the agent breached his or her duty to us, however, unless the court in which the proceeding is or was pending determines that the agent is fairly and reasonably entitled to indemnity for certain expenses. No indemnification is permitted where a settlement is reached without court approval.

Where permissive indemnification provisions control, indemnification may be authorized by a majority vote of the disinterested directors, by an independent legal counsel's written opinion, by our shareholders (the person to be indemnified is excluded from voting his or her shares) or by the court in which the proceeding is or was pending.

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Any provision in a California corporation's articles of incorporation, bylaws or shareholder or director resolution that indemnifies its officers or directors may prohibit permissive, but not mandatory, indemnification as described above. Such a provision must otherwise be consistent with Section 317. Nonetheless, a corporation has the power to purchase indemnity insurance for its agents even for situations in which it could not indemnify them. Insofar as indemnification for liabilities arising under the Securities Act may be permitted to directors, officers or persons controlling the Company pursuant to the foregoing provisions, we have been informed that in the opinion of the SEC such indemnification is against public policy as expressed in the Securities Act and is therefore unenforceable

### Item 10 - Executive Compensation

The following summary compensation table sets forth the aggregate cash compensation paid or accrued by our company to each of our executive officers and key employees for services rendered to our company during each of our fiscal years ended December 31, 2000 through December 31, 2004 and all plan and non-plan compensation awarded to, earned by or paid to certain designated executive officers:

#### SUMMARY COMPENSATION TABLE

(a) Name and Principal Position (1)	(b) Year	Annual Compensation			Long Term Compensation Awards		Payouts	
		(c) Salary (\$)	(d) Bonus (\$)	(e) Other Annual Compen- sation (\$)	(f) Restricted Stock Award(s) (\$)	(g) Securities Underlying Options/ SARs (f)	(h) LTIP Pay- outs	(i) All Other Compe satio
J.A. Fernandez, Sr., Chairman,	2000	\$ 59,202	\$0	\$0	\$0	\$0	\$0	\$0
	2001	\$ 50,859	\$0	\$0	\$0	\$0	\$0	\$0
	2002	\$ 77,770	\$0	\$0	\$0	\$0	\$0	\$0
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Director of Sales	2003	\$104,000	\$0	\$0	\$0	\$0	\$0	\$0
	2004	\$104,000	\$0	\$0	\$0	\$0	\$0	\$0
Andres F. Fernandez, President and Chief Executive Officer	2000	\$ 88,438	\$0	\$0	\$0	\$0	\$0	\$0
	2001	\$ 74,290	\$0	\$0	\$0	\$0	\$0	\$0
	2002	\$103,508	\$0	\$0	\$0	\$0	\$0	\$0
	2003	\$132,600	\$0	\$0	\$0	\$0	\$0	\$0
	2004	\$132,600	\$0	\$0	\$0	\$0	\$0	\$0
Emilio D. Jara, Vice- President Of Operations, Secretary	2000	\$ 36,400	\$0	\$0	\$0	\$0	\$0	\$0
	2001	\$ 42,500	\$0	\$0	\$0	\$0	\$0	\$0
	2002	\$ 43,000	\$0	\$0	\$0	\$0	\$0	\$0
	2003	\$ 52,000	\$0	\$0	\$0	\$0	\$0	\$0
	2004	\$ 52,000	\$0	\$0	\$0	\$0	\$0	\$0

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and  
Director

Amelia	2000	\$ 59,202	\$0	\$0	\$0	\$0	\$0	\$0
Fernandez,	2001	\$ 59,923	\$0	\$0	\$0	\$0	\$0	\$0
Vice President	2002	\$ 64,598	\$0	\$0	\$0	\$0	\$0	\$0
And	2003	\$ 78,702	\$50,000	\$0	\$0	\$0	\$0	\$0
Director	2004	\$ 78,702	\$0	\$0	\$0	\$0	\$0	\$0
Maria A.	2000	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Fernandez,	2001	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Director	2002	\$0	\$0	\$0	\$0	\$0	\$0	\$0
	2003	\$0	\$0	\$0	\$0	\$0	\$0	\$0
	2004	\$0	\$0	\$0	\$0	\$0	\$0	\$0

Compensation of Directors

We have no existing arrangements for compensating our directors for their attendance at meetings of the Board of Directors. Depending upon market forces and regulatory mandates, we may find it necessary to implement a formal compensation plan in future periods to obtain and retain qualified members of our Board of Directors.

Item 11 - Security Ownership of Certain Beneficial Owners and Management

The following table sets forth, as of March 24, 2005, the number of shares of Common Stock owned of record and beneficially by executive officers, directors and persons who hold 5% or more of the outstanding Common Stock of the Company. Also included are the shares held by all executive officers and directors as a group.

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Name and Address of Beneficial Owner	Shares Beneficially Owned	
	Number	Percent
Andres F. Fernandez	8,485,365	11.18%
J. A. Fernandez, Sr.	14,905,905	19.64%
Amelia C. Fernandez	4,281,900	5.64%
Maria A. Fernandez	260,000	*
Emilio D. Jara	54,250	*
Total common stock held by officers and directors as a group (4 people)	27,987,420	36.46%

\* Less than 1%

The contact address for each of our officers and directors is 3545 NW 71st Street, Miami, FL 33147.

Beneficial Ownership is determined in accordance with the rules of the

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Securities and Exchange Commission and generally includes voting or investment power with respect to securities. Shares of common stock subject to options or warrants currently exercisable or convertible, or exercisable or convertible within 60 days of January 5, 2005 are deemed outstanding for computing the percentage of the person holding such option or warrant but are not deemed outstanding for computing the percentage of any other person. J.A. Fernandez, Sr. and Amelia Fernandez are the father and mother of Andres and Maria Fernandez. The table above does not include the 384,500 shares Maria Fernandez holds as a Trustee for an Irrevocable Trust in which neither she nor any of the other Officers or Directors is the beneficial owner. However, the table does include the shares owned by Amelia Fernandez, who was an officer and director during 2003.

### Item 12 - Certain Relationships and Related Transactions

We lease our corporate office and manufacturing facility from our controlling stockholder under a long-term operating lease agreement. The lease requires a monthly payment of approximately \$5,735, including applicable State sales taxes. We are responsible for all utilities and maintenance expenses. The lease expires on December 1, 2009 and contains a clause that upon expiration, the Company and the controlling shareholder shall renegotiate the annual rental amount.

### Item 13 - Exhibits and Reports on Form 8-K.

(a) The exhibits required to be filed herewith by Item 601 of Regulation S-B, as described in the following index of exhibits, are incorporated herein by reference, as follows:

Exhibit No.	Description
31.1 *	Certification by Chief Executive Officer pursuant to 18 U.S.C. 1350.
32.1 *	Certification by Chief Financial Officer pursuant to 18 U.S.C. 1350.

\* Filed herewith

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### Item 14 - Principal Accountant Fees and Services

The Company paid or accrued the following fees in each of the prior two fiscal years to its principal accountant, S. W. Hatfield, CPA of Dallas, Texas.

### Item 14 - Principal Accountant Fees and Services

The Company paid or accrued the following fees in each of the prior two fiscal years to its principal accountant, S. W. Hatfield, CPA of Dallas, Texas.

Year ended	Year ended
December 31,	December 31,
2004	2003
-----	-----

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(1)	Audit fees	\$ 28,193	\$ 29,193
(2)	Audit-related fees	-	-
(3)	Tax fees	1,208	1,208
(4)	All other fees	-	-
		-----	-----
	Totals	\$ 29,401	\$ 29,401
		=====	=====

We have considered whether the provision of such non-audit services is compatible with S. W. Hatfield, CPA maintaining its independence and determined that these services do not compromise their independence.

Financial Information System Design and Implementation: S. W. Hatfield, CPA did not charge the Company any fees for financial information system design and implementation fees.

The Company has no formal audit committee. However, the entire Board of Directors (the "Board") is the Company's defacto audit committee. In discharging its oversight responsibility as to the audit process, the Board obtained from the independent auditors a formal written statement describing all relationships between the auditors and the Company that might bear on the auditors' independence as required by Independence Standards Board Standard No. 1, "Independence Discussions with Audit Committees." The Board discussed with the auditors any relationships that may impact their objectivity and independence, including fees for non-audit services, and satisfied itself as to the auditors' independence. The Board also discussed with management, the internal auditors and the independent auditors the quality and adequacy of the Company's internal controls.

The Company's principal accountant, S. W. Hatfield, CPA, did not engage any other persons or firms other than the principal accountant's full-time, permanent employees.

SIGNATURES

In accord with Section 13 or 15(d) of the Securities Act of 1933, as amended, the Company caused this report to be signed on its behalf by the undersigned, thereto duly authorized.

American Ammunition, Inc.

Dated: March , 2005  
-----

By: /s/ Andres F. Fernandez  
-----

Andres F. Fernandez  
President, Chief Executive Officer,  
Chief Financial Officer and Director

In accordance with the Securities Exchange Act of 1934, as amended, this report has been signed below by the following persons on behalf of the Company and in the capacities and on the date as indicated.



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Dated: March , 2005  
-----  
By: /s/ Andres F. Fernandez  
-----  
Andres F. Fernandez  
President, Chief Executive Officer,  
Chief Financial Officer and Director

Dated: March , 2005  
-----  
By: /s/ J.A. Fernandez, Sr.  
-----  
J. A. Fernandez, Sr.  
Chairman, Director of Sales,  
and Director

Dated: March , 2005  
-----  
By: /s/ Emilio D. Jara  
-----  
Emilio D. Jara.  
Vice President - Operations,  
Corporate Secretary and Director

Dated: March , 2005  
-----  
By: /s/ Maria A. Fernandez  
-----  
Maria A. Fernandez,  
Director

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### AMERICAN AMMUNITION, INC. AND SUBSIDIARIES

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Letterhead of S. W. Hatfield, CPA

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders  
American Ammunition, Inc.

We have audited the accompanying consolidated balance sheets of American Ammunition, Inc. (a California corporation) and Subsidiaries (Florida corporations) as of December 31, 2004 and 2003 and the related consolidated statements of operations and comprehensive loss, changes in stockholders' equity and cash flows for each of the two years ended December 31, 2004 and 2003, respectively. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of American Ammunition, Inc. and Subsidiaries as of December 31, 2004 and 2003 and the results of their consolidated operations and consolidated cash flows for each of the two years ended December 31, 2004 and 2003, respectively, in conformity with accounting principles generally accepted in the United States of America.

/s/ S.W. Hatfield

-----  
S. W. HATFIELD, CPA

Dallas, Texas  
March 11, 2005

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AMERICAN AMMUNITION, INC.  
CONSOLIDATED BALANCE SHEETS  
December 31, 2004 and 2003

	December 31, 2004	December 31, 2003
	-----	-----
ASSETS		
Current Assets		
Cash on hand and in bank	\$ 805,465	\$ 505,671
Accounts receivable - trade, net of allowance for doubtful accounts of \$-0- and \$-0-, respectively	639,444	520,835
Inventory	912,424	1,112,756
Prepaid expenses	58,847	40,388
	-----	-----
Total Current Assets	2,416,180	2,179,650
	-----	-----
Property and Equipment - at cost or contributed value		
Manufacturing equipment	7,976,248	7,131,233
Office furniture and fixtures	69,889	62,893
Leasehold improvements	184,939	184,690
	-----	-----
Accumulated depreciation	8,231,076 (4,801,695)	7,378,816 (4,066,390)
	-----	-----
Net Property and Equipment	3,429,381	3,312,426
	-----	-----
Other Assets		
Patents, Trademarks and Noncompetition agreement, net of accumulated amortization of approximately \$9,190	266,500	-
Deposits and other	83,660	77,860
	-----	-----
Total Other Assets	350,160	77,860
	-----	-----
TOTAL ASSETS	\$ 6,195,721	\$ 5,569,936
	=====	=====

- Continued -

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

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AMERICAN AMMUNITION, INC.  
CONSOLIDATED BALANCE SHEETS - CONTINUED  
December 31, 2004 and 2003

	December 31, 2004	December 31, 2003
LIABILITIES AND STOCKHOLDERS' EQUITY		
<b>Current Liabilities</b>		
Current maturities of leases payable	\$ -	\$ 7,841
Customer deposits	440,906	4,100
Accounts payable - trade	936,885	128,865
Accrued salaries and wages	135,970	-
Accrued interest payable	15,000	-
Accrued dividends payable	15,899	11,020
	-----	-----
Total Liabilities	1,544,660	151,826
	-----	-----
 <b>Commitments and Contingencies</b>		
 Mandatory Convertible Debenture	 266,365	 391,365
	-----	-----
 <b>Stockholders' Equity</b>		
Preferred stock - \$0.001 par value 20,000,000 shares authorized. 1,795,320 shares allocated to Series A 91,700 shares allocated to Series B 1,905,882 shares allocated to Series C	2,010	104
Common stock - \$0.001 par value. 300,000,000 shares authorized. 74,851,691 and 66,893,628 shares issued and outstanding	74,852	66,894
Additional paid-in capital	24,472,709	21,588,791
Accumulated deficit	(19,989,875)	(16,629,044)
	-----	-----
Stock subscription receivable	4,559,696 (175,000)	5,026,745 -
	-----	-----
Total Stockholders' Equity	4,384,696	5,026,745
	-----	-----
 <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	 \$ 6,195,721	 \$ 5,569,936

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

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AMERICAN AMMUNITION, INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS  
Years ended December 31, 2004 and 2003

	Year ended December 31, 2004	Year ended December 31, 2003
	-----	-----
Revenues	\$ 3,247,368	\$ 1,984,997
	-----	-----
Cost of Sales		
Materials	2,383,198	1,355,098
Direct Labor	836,386	868,004
Other direct costs and expenses	671,787	340,346
Depreciation	729,295	668,574
	-----	-----
Total Cost of Sales	4,620,666	3,232,022
	-----	-----
Gross Profit	(1,373,298)	(1,247,025)
	-----	-----
Operating Expenses		
Research and development expenses	11,457	4,038
Marketing and promotion expenses	440,248	115,767
Salaries, wages and related expenses	365,633	399,710
Other operating expenses	718,610	567,700
Interest expense	16,005	35,154
Depreciation expense	6,009	4,516
Amortization of intangibles	9,190	-
Compensation expense related to common stock issuances at less than "fair value"	381,902	882,291
	-----	-----
Total Operating Expenses	1,949,054	2,009,176
	-----	-----
Loss from Operations	(3,322,352)	(3,256,201)
Other Income (Expense)		
Other income (expense)	4,279	63,382
Gain on forgiveness of accounts payable	-	339,202
Gain on sale of equipment	-	7,900
Amortization of Beneficial Conversion		

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Feature Discount on Preferred Stock	-	(93,678)
	-----	-----
Loss before Income Taxes	(3,318,073)	(2,939,395)
Provision for Income Taxes	-	-
	-----	-----
Net Loss	(3,318,073)	(2,939,395)
Other Comprehensive Income	-	-
	-----	-----
Comprehensive Loss	(3,318,073)	(2,939,395)
Preferred Stock Dividends	(42,758)	(28,931)
	-----	-----
Net Loss available to Common Shareholders	\$ (3,360,831)	\$ (2,968,326)
	=====	=====
Loss per weighted-average share of common stock outstanding, computed on net loss - basic and fully diluted	\$ (0.05)	\$ (0.05)
	=====	=====
Weighted-average number of common shares outstanding	71,814,490	61,202,839
	=====	=====

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

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AMERICAN AMMUNITION, INC.  
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY  
Years ended December 31, 2004 and 2003

	Mandatory Preferred Stock		Convertible Common Stock		Additional paid-in capital	Accu
	Shares	Amount	Shares	Amount	capital	d
	-----	-----	-----	-----	-----	-----
Balances at January 1, 2003	41,000	\$ 41	55,328,166	\$55,329	\$16,728,123	\$(13
Issuance of preferred stock for cash	91,700	92	-	-	458,408	
Less costs of raising capital	-	-	-	-	(45,850)	
Issuance of common stock for Cash	-	-	4,552,183	4,552	1,179,630	
Conversion of debenture	-	-	4,561,753	4,562	1,086,364	
Exercise of warrant for cash	-	-	2,086,350	2,086	2,084,264	
Payment of preferred stock dividends	-	-	46,176	46	20,464	
Conversion of preferred stock	(29,000)	(29)	319,000	319	(290)	
Costs of acquiring convertible debenture	-	-	-	-	(16,000)	
Beneficial Conversion Discount						
Feature on preferred stock	-	-	-	-	93,678	
Dividends declared on Preferred Stock	-	-	-	-	-	
Net loss for the year	-	-	-	-	-	(2
	-----	-----	-----	-----	-----	-----

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Balances at December 31, 2003	62,700	104	66,893,628	66,894	21,588,791	(16
Issuance of preferred stock for cash	1,905,882	1,906	-	-	322,094	
Issuance of common stock for Cash	-	-	1,500,000	1,500	1,498,500	
Less subscription receivable	-	-	-	-	-	
Conversion of debenture	-	-	4,900,000	4,900	501,100	
Less subscription receivable	-	-	-	-	-	
Payment of costs to acquire capital	-	-	300,000	300	59,700	
Less cost of capital	-	-	-	-	(36,000)	
Acquisition of assets	-	-	1,111,112	1,111	498,889	
Payment of preferred stock dividends	-	-	146,952	147	39,635	
Dividends declared on Preferred Stock	-	-	-	-	-	
Net loss for the year	-	-	-	-	-	(3
	-----	-----	-----	-----	-----	-----
Balances at December 31, 2004	2,009,582	\$2,010	74,851,692	\$74,852	\$24,472,709	\$(19
	=====	=====	=====	=====	=====	=====

Stock subscription receivable at December 31, 2004

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

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AMERICAN AMMUNITION, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
Years ended December 31, 2004 and 2003

	Year ended December 31, 2004	Year ended December 31, 2003
	-----	-----
Cash flows from operating activities		
Net loss for the year	\$ (3,318,073)	\$ (2,939,395)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation and amortization	744,494	673,090
Bad debt expense	85,490	2,522
Acquisition of inventory with common stock	89,510	-
Gain on forgiveness of accounts payable	-	(339,202)
Gain on sale of equipment	-	(7,900)
Amortization of conversion discount on preferred stock	-	93,678
Compensation expense related to common stock issuances at less than "fair value"	381,902	882,291
(Increase) Decrease in		
Accounts receivable	(204,099)	(492,069)
Inventory	200,332	(727,942)

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Prepaid expenses, deposits and other	(24,258)	(20,997)
Increase (Decrease) in		
Accounts payable and other accrued liabilities	808,023	53,157
Accrued payroll payable	135,970	(18,709)
Accrued interest payable	15,000	-
Customer deposits	436,806	(76,853)
	-----	-----
Net cash provided by (used in) operating activities	(648,903)	(2,918,329)
	-----	-----
Cash flows from investing activities		
Cash received on sale of equipment	-	7,900
Purchase of property and equipment	(717,462)	(288,891)
	-----	-----
Net cash used in investing activities	(717,462)	(280,991)
	-----	-----
Cash flows from financing activities		
Principal paid on long-term debt	-	(450,000)
Principal paid on long-term capital leases	(7,841)	(9,507)
Cash received on sale of Preferred Stock	324,000	458,500
Cash received on issuance of Mandatory Convertible Debenture	1,350,000	350,000
Cash received on sale of common stock	-	3,260,532
Cash paid to acquire capital	-	(61,850)
	-----	-----
Net cash provided by financing activities	1,666,159	3,547,675
	-----	-----
INCREASE (DECREASE) IN CASH	299,794	348,355
Cash at beginning of year	505,671	157,316
	-----	-----
Cash at end of year	\$ 805,465	\$ 505,671
	=====	=====

- Continued -

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

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AMERICAN AMMUNITION, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS - CONTINUED  
Years ended December 31, 2004 and 2003

	Year ended December 31, 2004	Year ended December 31, 2003
	-----	-----
Supplemental disclosure of interest and income taxes paid		



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Interest paid for the period	\$ 1,005	\$ 26,170
	=====	=====
Income taxes paid for the period	\$ -	\$ -
	=====	=====
Supplemental disclosure of non-cash investing and financing activities		
Conversion of debt into common stock	\$ 125,000	\$ 208,635
	=====	=====
Payment of accrued dividends on preferred stock with common stock	\$ 37,878	\$ 30,511
	=====	=====
Acquisition of equipment and intangibles with common stock	\$ 410,490	\$ -
	=====	=====

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

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note A - Organization and Description of Business

American Ammunition, Inc. (AAI or Company) was incorporated on February 1, 2000 in accordance with the Laws of the State of California. The Company functions as a holding company providing management oversight services to it's wholly-owned operating subsidiaries; F&F Equipment, Inc. and Industrial Plating Enterprise Co.

F&F Equipment, Inc.(F&F) was incorporated on October 4, 1983 in accordance with the Laws of the State of Florida. F&F is engaged in the design, manufacture and international sales of small arms ammunition. F&F has conducted its business operations under the assumed name of "American Ammunition" since its inception.

Industrial Plating Enterprise Co. (IPE), which was incorporated and commenced production on June 14, 2002. IPE is a fully licensed and approved state of the art electrochemical metallization facility for processing the Company's line of

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small arms projectiles as well as other products and services while employing environmentally sound water conservation and proven waste treatment techniques. The facility meets or exceeds all current environmental requirements and enjoys the "conditionally exempt small quantity generator" status for State and Federal regulations. All activities of IPE since it's inception have been dedicated to the needs and demands of F&F.

### Note B - Preparation of Financial Statements

The Company and its subsidiaries follow the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America and have adopted a year-end of December 31 for all entities.

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 assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Management further acknowledges that it is solely responsible for adopting sound accounting practices, establishing and maintaining a system of internal accounting control and preventing and detecting fraud. The Company's system of internal accounting control is designed to assure, among other items, that 1) recorded transactions are valid; 2) valid transactions are recorded; and 3) transactions are recorded in the proper period in a timely manner to produce financial statements which present fairly the financial condition, results of operations and cash flows of the Company for the respective periods being presented

For segment reporting purposes, the Company operated in only one industry segment during the periods represented in the accompanying financial statements and makes all operating decisions and allocates resources based on the best benefit to the Company as a whole.

The accompanying consolidated financial statements contain the accounts of American Ammunition, Inc. and its wholly-owned subsidiaries, F&F Equipment, Inc. and Industrial Plating Enterprise Co. All significant intercompany transactions have been eliminated. The consolidated entities are collectively referred to as "Company".

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

### Note C - Summary of Significant Accounting Policies

#### 1. Cash and cash equivalents

For Statement of Cash Flows purposes, the Company considers all cash on hand and in banks, certificates of deposit and other highly-liquid investments with maturities of three months or less, when purchased, to be

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cash and cash equivalents.

Cash overdraft positions may occur from time to time due to the timing of making bank deposits and releasing checks, in accordance with the Company's cash management policies.

### 2. Accounts receivable and Revenue Recognition

In the normal course of business, the Company extends unsecured credit to virtually all of its customers which are located throughout the United States. Because of the credit risk involved, management has provided an allowance for doubtful accounts which reflects its opinion of amounts which will eventually become uncollectible. In the event of complete non-performance, the maximum exposure to the Company is the recorded amount of trade accounts receivable shown on the balance sheet at the date of non-performance.

The Company ships all product on an FOB-Plant, "as-is" basis. Accordingly, revenue is recognized by the Company at the point at which an order is shipped at a fixed price, collection is reasonably assured and the Company has no remaining performance obligations related to the sale. The Company sells all products with "no right of return" by the purchaser for any factor other than defects in the product's production.

On rare occasion, the Company may elect to accept product returns from customers on a case-by-case basis to offset unpaid accounts receivable. These situations are a "last case" scenario and are initiated by senior management through negotiations with the respective customer.

### 3. Inventory

Inventory consists of raw materials, work-in-process and finished goods related to the production and sale of small arms ammunition. Inventory is valued at the lower of cost or market using the first-in, first-out method.

### 4. Property, plant and equipment

Property and equipment are recorded at historical cost. These costs are depreciated over the estimated useful lives of the individual assets using the straight-line method, generally three to ten years.

Gains and losses from disposition of property and equipment are recognized as incurred and are included in operations.

### 5. Income Taxes

The Company uses the asset and liability method of accounting for income taxes. At December 31, 2004 and 2003, the deferred tax asset and deferred tax liability accounts, as recorded when material to the financial statements, are entirely the result of temporary differences. Temporary differences represent differences in the recognition of assets and liabilities for tax and financial reporting purposes, primarily accumulated depreciation and amortization, allowance for doubtful accounts and vacation accruals.

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AMERICAN AMMUNITION, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

### Note C - Summary of Significant Accounting Policies - Continued

#### 5. Income Taxes - continued

As of December 31, 2004 and 2003, the deferred tax asset related to the Company's net operating loss carryforward is fully reserved. If these carryforwards are not utilized, they will begin to expire in 2005.

#### 6. Earnings (loss) per share

Basic earnings (loss) per share is computed by dividing the net income (loss) available to common shareholders by the weighted-average number of common shares outstanding during the respective period presented in our accompanying financial statements.

Fully diluted earnings (loss) per share is computed similar to basic income (loss) per share except that the denominator is increased to include the number of common stock equivalents (primarily outstanding options and warrants).

Common stock equivalents represent the dilutive effect of the assumed exercise of the outstanding stock options and warrants, using the treasury stock method, at either the beginning of the respective period presented or the date of issuance, whichever is later, and only if the common stock equivalents are considered dilutive based upon the Company's net income (loss) position at the calculation date.

As of December 31, 2004 and 2003, and subsequent thereto, the Company had no options outstanding. The outstanding warrants and convertible preferred stock and mandatorily convertible debentures are anti-dilutive due to the Company's net operating loss position.

#### 7. Advertising costs

The Company does not conduct any direct response advertising activities. For non-direct response advertising, the Company charges the costs of these efforts to operations at the first time the related advertising is published.

### Note D - Fair Value of Financial Instruments

The carrying amount of cash, accounts receivable, accounts payable and notes payable, as applicable, approximates fair value due to the short term nature of these items and/or the current interest rates payable in relation to current market conditions.

Interest rate risk is the risk that the Company's earnings are subject to fluctuations in interest rates on either investments or on debt and is fully dependent upon the volatility of these rates. The Company does not use derivative instruments to moderate its exposure to interest rate risk, if any.

Financial risk is the risk that the Company's earnings are subject to fluctuations in interest rates or foreign exchange rates and are fully dependent upon the volatility of these rates. The company does not use derivative instruments to moderate its exposure to financial risk, if any.

AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Note E - Inventory

As of December 31, 2004 and 2003, inventory consisted of the following components:

	December 31, 2004	December 31, 2003
	-----	-----
Raw materials	\$ 522,585	\$ 539,474
Work in process	306,360	360,450
Finished goods	83,479	212,832
	-----	-----
Totals	\$ 912,424 =====	\$ 1,112,756 =====

Note F - Property and Equipment

Property and equipment consist of the following components:

	December 31, 2004	December 31, 2003	Estimated useful life
	-----	-----	
Manufacturing equipment	\$ 7,745,112	\$ 7,131,233	3-10 years
Office furniture and fixtures	69,889	62,893	3- 7 years
Leasehold improvements	184,939	184,690	8-20 years
	-----	-----	
	7,999,940	7,378,816	
Accumulated depreciation	(4,762,074)	(4,066,390)	
	-----	-----	
Net property and equipment	\$ 3,237,866 =====	\$ 3,312,426 =====	

Total depreciation expense charged to operations for the years ended December 31, 2004 and 2003 was approximately \$717,349 and \$673,090, respectively.

Note G - Capital Leases Payable

Capital leases payable consist of the following as of December 31, 2004 and 2003, respectively:

December 31,      December 31,

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	2004	2003
	-----	-----
Three separate capital leases payable to various equipment financing companies. Interest ranging between 11.37% and 14.05%. Payable in aggregate monthly installments of approximately \$935, including interest. Final maturities occurred between September 2004 and December 2004.	\$ -	\$ 7,841
Less current maturities	-	(7,841)
	-----	-----
Long-term portion	\$ -	\$ -
	=====	=====

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Note H - Convertible Debenture

The Company entered into a Securities Purchase Agreement with La Jolla Cove Investors, Inc. ("La Jolla") on October 4, 2002 for the sale of (i) \$250,000 in convertible debentures and (ii) warrants to buy 30,000,000 shares of our common stock. On March 13, 2003 and May 6, 2003, La Jolla advanced an aggregate of \$350,000 to our company which such funding was allocated towards the principal balance of our convertible debentures.

As of December 31, 2004, the outstanding balance on the convertible debenture is approximately \$266,365 and we have approximately 2,663,650 warrants outstanding.

The debentures bear interest at 8%, mature on June 30, 2006, and are convertible into our common stock, at the selling stockholder's option. The convertible debentures are convertible into the number of our shares of common stock equal to the principal amount of the debentures being converted multiplied by 11, less the product of the conversion price multiplied by 10 times the dollar amount of the debenture. The conversion price for the convertible debentures is the lesser of (i) \$1.00 or (ii) seventy six percent of the average of the five lowest volume weighted average prices during the twenty (20) trading days prior to the conversion. Accordingly, there is in fact no limit on the number of shares into which the debenture may be converted. However, in the event that our market price is less than \$.30, we will have the option to prepay the debenture at 125% rather than have the debenture converted. In addition, the selling stockholder is obligated to exercise the warrant concurrently with the submission of a conversion notice by the selling stockholder. As of December 31, 2004, the warrant is exercisable into 2,663,650 shares of common stock at an exercise price of \$1.00 per share.

In December 2004, we entered into an addendum to the convertible debenture and warrant whereby the Company agreed to the following:

\* the discount multiplier was reduced from eighty percent to seventy six

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- percent;
- \* within five business days after this registration statement being declared effective, La Jolla is required to submit a debenture conversion in the amount of \$10,000 and every ten business days thereafter La Jolla shall submit three additional debenture conversion in the amount of \$10,000 each;
  - \* within five business days after this registration statement being declared effective, La Jolla shall wire \$400,000 to us as a prepayment towards the exercise of its warrant; and
  - \* immediately following the sale of all shares held by La Jolla in connection with the debenture conversions in the aggregate amount of \$40,000, La Jolla shall wire \$275,000 to us as a prepayment towards the exercise of its warrant and shall submit a debenture conversion in the amount of \$6,250 on the first business day of each month until the debenture is no longer outstanding.

LaJolla has contractually agreed to restrict its ability to convert or exercise its warrants and receive shares of our common stock such that the number of shares of common stock held by them and their affiliates after such conversion or exercise does exceed 4.9% of the then issued and outstanding shares of common stock.

Due to the contractually agreed mandatory conversion of this Debenture, the Company has reflected this transaction in its balance sheet as a "mezzanine" level debt obligation on its balance sheet, between "Total Liabilities" and "Stockholders' Equity". Upon the respective mandatory conversion, the Company will relieve the respective portion of the Debenture and the any related accrued, but unpaid interest, and credit this amount to the respective "common stock" and "additional paid-in capital" accounts in the stockholder's equity section for the par value and excess amount over the par value of the respective shares issued.

As the warrant is non-detachable from the Debenture and requires simultaneous exercise upon conversion of the Debenture, no value was assigned to the issued warrant. Upon exercise of the warrant, the Company will record the issuance of the underlying shares as a new issuance of common stock on the date of each respective exercise.

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Note H - Convertible Debenture - continued

On various dates through December 31, 2003, the Debenture Holder elected to convert an aggregate \$208,635, through 24 separate transactions, in outstanding Debenture principal into restricted, unregistered common stock. This election caused the Company to issue 4,561,753 shares of restricted, unregistered common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 2,086,350 shares of the Company's restricted, unregistered common stock for gross proceeds of \$2,086,350.

On various dates between January 1, 2004 and December 31, 2004, the Debenture Holder elected to convert an aggregate \$150,000, through 6 separate

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transactions, in outstanding Debenture principal into registered common stock. This election caused the Company to issue 4,900,000 shares of common stock to the Debenture Holder. Additionally, pursuant to the contract terms, the Debenture Holder concurrently exercised a portion of the outstanding Warrant to purchase 1,500,000 shares of the Company's common stock for gross proceeds of \$1,500,000. As of December 31, 2004, an aggregate of 1,000,000 shares of the Company's common stock have been issued by the Company and are being held in escrow by the Company's counsel pending receipt of the final \$150,000 from the Debenture Holder.

### Note I - Preferred Stock Transactions

Preferred stock consists of the following as of December 31, 2004 and 2003, respectively:

	December 31, 2004		December 31, 2003	
	# shares	value	# shares	value
Series A Cumulative				
Convertible Preferred Stock	12,000	\$ 60,000	12,000	\$ 60,000
Series B Cumulative				
Convertible Preferred Stock	91,700	458,500	91,700	458,500
Series C Convertible Preferred Stock	1,905,882	324,000	-	-
	2,009,582	\$842,500	103,700	\$518,500
	=====	=====	=====	=====

#### Series A Convertible Preferred Stock

In September, October and November 2001, the Company sold an aggregate 222,600 shares of \$5.00 Series A Convertible Preferred Stock (Series A Preferred Stock) for total proceeds of approximately \$1,113,000 through a Private Placement Memorandum. The Series A Convertible Preferred Stock provides for cumulative dividends at a rate of 8.0% per year, payable quarterly, in cash or shares of the Company's common stock at the Company's election. Each share of Series A Preferred Stock is convertible into 11 shares of the Company's common stock initially at any time after 6 months of the date of issue and prior to the notice of redemption at the option of the holder, subject to adjustments for customary anti-dilution events. In December 2001, at the request of the holders of the Series A Preferred Stock, the Company and the individual holders modified the holding period for conversion to allow for conversion in December 2001.

In September 2001, the Company's principal stockholder converted approximately \$4,007,327 of unsecured debt and approximately \$3,546,273 of cumulative and unpaid accrued interest into 1,510,710 shares of Series A Preferred Stock.

In September 2001, a creditor of the Company agreed to convert approximately \$10,000 of trade accounts payable into 2,000 shares of Series A Preferred Stock.

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED



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### Note I - Preferred Stock Transactions - Continued

#### Series A Convertible Preferred Stock - continued

In December 2001, concurrent with a modification in the holding period prior to conversion, certain holders of the Series A Preferred Stock orally notified the Company of their intent to exercise the conversion features on 1,749,720 issued and outstanding shares of Series A Preferred Stock into 19,246,920 shares of common stock prior to December 31, 2001. Due to the timing of the requisite documentation, the clerical activities related to this conversion were not completed until February 2002.

In conjunction with the Series A Preferred Stock, certain shares were sold after the Company's common stock was approved for trading by the National Association of Securities Dealers on the OTC Bulletin Board in October 2001. The shares of Series A Preferred Stock sold subsequent to this date had an equivalent per share value of common stock below the ending quoted market price of the Company's common stock on their respective issue dates. This difference created a Beneficial Conversion Feature Discount of approximately \$1,207,993. This discount was then amortized over the unexpired time period between the date of issue of the eligible shares and the eligible conversion date, as amended. All of the shares sold subsequent to the initial trading date were converted in December 2001 and, accordingly, the approximate \$1,207,993 in Beneficial Conversion Feature Discount was fully amortized to operations.

In December 2002, a holder of 5,000 shares of Series A Preferred Stock exercised his conversion rights and converted these shares of Series A Preferred Stock into 55,000 shares of restricted, unregistered common stock.

In January 2003, three separate holders of 9,000 shares of Series A Preferred Stock exercised their conversion rights and converted these shares of Series A Preferred stock into 99,000 shares of restricted, unregistered common stock.

#### Series B Convertible Preferred Stock

In May 2003, the Company sold an aggregate 91,700 shares of \$5.00 Series B Convertible Preferred Stock (Series B Preferred Stock) for total proceeds of approximately \$458,500 through a separate Private Placement Memorandum. The Series B Convertible Preferred Stock provides for cumulative dividends at a rate of 8.0% per year, payable quarterly, in cash or shares of the Company's common stock at the Company's election. Each share of Series B Preferred Stock is convertible into 11 shares of the Company's common stock initially at any time after 6 months of the date of issue and prior to the notice of redemption at the option of the holder, subject to adjustments for customary anti-dilution events.

#### Series C Convertible Preferred Stock

In November 2004, the Company sold 1,905,882 shares of Series C Convertible Preferred Stock to an existing shareholder and officer of the Company in a private transaction pursuant to Section (4)2 of the Securities Act of 1933 for gross proceeds of approximately \$324,000. No underwriter was used in conjunction with this transaction.

The Series C Convertible Preferred Stock provides for dividends at a rate of 4.0% per annum, to be declared and paid monthly in either cash or stock at the discretion of the Company.

The Series C Preferred Stock is convertible at a rate of \$0.18 per share into 1,800,000 shares of the Company's common stock at any time at the option of the holder, subject to adjustments for customary anti-dilution events.

AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Note K - Common Stock Transactions

In January 2003, the Company issued an aggregate 937,568 shares of restricted, unregistered common stock for cash proceeds of approximately \$324,182. These sales were made at a price of either \$0.23 or \$0.36 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The proceeds of this transaction were used for operating working capital.

In February 2003, the Company issued 384,615 shares of restricted, unregistered common stock for cash proceeds of approximately \$100,000. These sales were made at a price of \$0.26 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The proceeds of this transaction were used to reduce the Company's outstanding long-term debt.

In March 2003, the Company issued 972,222 shares of restricted, unregistered common stock for cash proceeds of approximately \$350,000. These sales were made at a price of \$0.36 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The proceeds of this transaction were used to reduce the Company's outstanding long-term debt.

In March 2003, the Company issued an aggregate 966,608 shares of restricted, unregistered common stock to the Holder of the Company's 8.0% Convertible Debenture upon notice of conversion of \$35,000 of outstanding principal and exercise of a portion of the outstanding warrant to purchase 350,000 shares of common stock. This transaction was valued at \$385,000, or approximately \$0.40 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The cash proceeds of this transaction were used to provide working capital and support operations.

In May 2003, the Company issued 1,967 shares of restricted, unregistered common stock in payment of approximately \$1,200 in accrued dividends payable on the Company's outstanding Series A Preferred Stock for the quarter ended March 31, 2003.

During the period from July 1, 2003 through September 30, 2003, the Company issued an aggregate 2,902,129 shares of common stock, in 15 separate transactions, in exchange for the redemption of approximately \$93,500 in outstanding debenture balance and approximately \$935,000 in cash from the exercise of the affiliated warrant. Where the closing price of the Company's common stock was in excess of the respective price per share on the respective transaction date, the Company recognized a charge to operations for "compensation expense related to common stock issuances at less than "fair

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value". The cumulative effect of transactions where the transaction price, as established in the Debenture Agreement, was less than the closing price on the date of the respective transactions resulted in a cumulative charge to operations of approximately \$317,539 during this time period.

In October 2003, in a separate transaction, the Company sold 2,200,000 shares of restricted, unregistered common stock to the Debenture Holder for cash proceeds of approximately \$400,000, or approximately \$0.18 per share, which was in excess of the discounted "fair value" of the Company's common stock based on the quoted closing price of the Company's common stock on the date of the respective transaction. The cash proceeds of this transaction were used to provide working capital and support operations.

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### AMERICAN AMMUNITION, INC.

#### NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

##### Note K - Common Stock Transactions - Continued

In October 2003, the Company issued an aggregate 1,659,847 shares of common stock, in 3 separate transactions, in exchange for the redemption of approximately \$40,000 in outstanding debenture balance and approximately \$400,000 in cash from the exercise of the affiliated warrant. Where the closing price of the Company's common stock was in excess of the respective price per share on the respective transaction date, the Company recognized a charge to operations for "compensation expense related to common stock issuances at less than "fair value". The cumulative effect of transactions where the transaction price, as established in the Debenture Agreement, was less than the closing price on the date of the respective transactions resulted in a cumulative charge to operations of approximately \$146,189 during this time period.

In October 2003, the Company issued an aggregate 37,866 shares of restricted, unregistered common stock in payment of approximately \$16,710 in accrued dividends payable on the Company's outstanding Series A and Series B Preferred Stock for the quarters ended June 30, 2003 and September 30, 2003, collectively.

In January 2004, the Company issued 38,038 shares of restricted, unregistered common stock in payment of approximately \$10,000 in accrued dividends payable on the Company's outstanding Series A and Series B Preferred Stock for the quarter ended December 31, 2003. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

During the period from January 1, 2004 through March 31, 2004, the Company issued an aggregate 2,400,000 shares of common stock, in two (2) separate transactions, in exchange for the redemption of approximately \$50,000 in outstanding debenture balance and approximately \$500,000 in cash from the exercise of the affiliated warrant. Where the closing price of the Company's common stock was in excess of the respective price per share on the respective transaction date, the Company recognized a charge to operations for "compensation expense related to common stock issuances at less than "fair value". The cumulative effect of transactions where the transaction price, as established in the Debenture Agreement, was less than the closing price on the date of the respective transactions resulted in a cumulative charge to

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operations of approximately \$321,000 during this time period.

In May 2004, the Company issued 25,260 shares of restricted, unregistered common stock in payment of approximately \$9,170 in accrued dividends payable on the Company's outstanding Series B Preferred Stock for the quarter ended March 31, 2004. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

During the period from April 1, 2004 through June 30, 2004, the Company issued an aggregate 3,000,000 shares of common stock, in three (3) separate transactions, in exchange for the redemption of approximately \$75,000 in outstanding debenture balance and approximately \$750,000 in cash from the exercise of the affiliated warrant. Where the closing price of the Company's common stock was in excess of the respective price per share on the respective transaction date, the Company recognized a charge to operations for "compensation expense related to common stock issuances at less than "fair value". The cumulative effect of transactions where the transaction price, as established in the Debenture Agreement, was less than the closing price on the date of the respective transactions resulted in a cumulative charge to operations of approximately \$35,000 during this time period. Additionally, on June 29, 2004, the Company issued an additional 1,000,000 shares of common stock in advance of the exercise of a \$25,000 redemption on the outstanding debenture payable and a \$250,000 cash payment on the exercise of the affiliated warrant. As of December 31, 2004, the Company has received \$100,000 in cash on the warrant exercise and has not applied the debt reduction portion of this transaction.

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

### Note K - Common Stock Transactions - Continued

On May 26, 2004, the Company issued 300,000 shares of restricted, unregistered common stock to two separate corporations in payment and full satisfaction of all amounts due for fees and/or commissions due in conjunction with the Company's convertible debenture financing transaction. This transaction was valued at approximately \$36,000, which was less than the closing price on the date of the respective transaction resulted in a charge to operations of approximately \$24,000. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

In August 2004, the Company issued 29,746 shares of restricted, unregistered common stock in payment of approximately \$9,170 in accrued dividends payable on the Company's outstanding Series B Preferred Stock for the quarter ended June 30, 2004. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

On October 19, 2004, the Company issued 1,111,112 shares of restricted, unregistered common stock to acquire certain assets valued at an aggregate \$500,000. The assets consist principally of equipment (approximately \$134,000),

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inventory (approximately \$89,500) and patents and a covenant not-to-compete (approximately \$276,500).

In November 2004, the Company issued 53,908 shares of restricted, unregistered common stock in payment of approximately \$9,170 in accrued dividends payable on the Company's outstanding Series B Preferred Stock for the quarter ended June 30, 2004. The Company relied upon Section 4(2) of the Securities Act of 1933, as amended, for an exemption from registration of these shares and no underwriter was used in this transaction.

### Note L - Rental Commitments

The Company leases its corporate office and manufacturing facility from its controlling stockholder under a long-term operating lease agreement. The lease requires a monthly payment of approximately \$5,735, including applicable sales taxes. The Company is responsible for all utilities and maintenance expenses. The lease expires on December 1, 2009 and contains a clause that upon expiration, the Company and the controlling shareholder shall renegotiate the annual rental amount.

The Company's subsidiary, IPE, leases its manufacturing facility from an unrelated third-party under a long-term operating lease agreement. This lease is for a period of five (5) years and requires graduated monthly payments, changing on the lease anniversary date, ranging from approximately \$1,751 to \$1,914, plus the applicable sales taxes. The Company is responsible for all utilities and maintenance expenses. The lease expires on February 28, 2007 and may be renewed for an additional five (5) year term at a rental rate of approximately \$1,971, plus applicable sales taxes for the first renewal year and 3.0% increase on each succeeding anniversary date. Total rent expense under this lease was approximately \$20,752 and \$16,622, respectively, for each of the years ended December 31, 2004 and 2003.

In May 2004, the Company entered into a long-term lease agreement for a warehouse facility adjacent to the Company's primary office and manufacturing facility. This lease is for a period of two (2) years and requires payments of approximately \$6,206 per month for the first 12 months and approximately \$6,393 for the second 12 months, plus applicable sales taxes. The Company is responsible for all utilities and maintenance expenses. This lease expires on May 31, 2006. Further, the Company is responsible for any incremental real estate taxes and property insurance in excess of the amounts incurred by the landlord for the calendar year immediately preceding the execution of the lease.

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Note L - Rental Commitments - Continued

Future minimum rental payments on the above leases are as follows:

Year ended	
December 31,	Amount
-----	-----

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2005	\$166,974
2006	117,244
2007	72,643
2008	68,815
2007	68,815
	-----
Totals	\$494,491
	=====

For the respective years ended December 31, 2004, the Company paid an aggregate of \$131,804 and \$87,826 for rent under these agreements.

Note M - Income Taxes

The components of income tax (benefit) expense for the years ended December 31, 2004 and 2003, respectively, are as follows:

	Year ended December 31, 2004	Year ended December 31, 2003
	-----	-----
Federal:		
Current	\$ -	\$ -
Deferred	-	-
	-----	-----
	-	-
	-----	-----
State:		
Current	-	-
Deferred	-	-
	-----	-----
	-	-
	-----	-----
Total	\$ -	\$ -
	=====	=====

As of December 31, 2004, the Company has a net operating loss carryforward of approximately \$7,850,000 to offset future taxable income. Subject to current regulations, components of this carryforward will begin to expire in 2003. The amount and availability of the net operating loss carryforwards may be subject to limitations set forth by the Internal Revenue Code. Factors such as the number of shares ultimately issued within a three year look-back period; whether there is a deemed more than 50 percent change in control; the applicable long-term tax exempt bond rate; continuity of historical business; and subsequent income of the Company all enter into the annual computation of allowable annual utilization of the carryforwards.

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AMERICAN AMMUNITION, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

### Note M - Income Taxes - Continued

The Company's income tax expense (benefit) for the years ended December 31, 2004 and 2003, respectively, differed from the statutory federal rate of 34 percent as follows:

	Year ended December 31, 2004	Year ended December 31, 2003
	-----	-----
Statutory rate applied to loss before income taxes	\$(1,128,000)	\$ (999,000)
Increase (decrease) in income taxes resulting from:		
State income taxes	-	-
Other, including reserve for deferred tax asset	1,128,000	999,000
	-----	-----
Income tax expense	\$ -	\$ -
	=====	=====

Temporary differences, consisting primarily of the net operating loss carryforward and statutory differences in the depreciable lives for property and equipment, between the financial statement carrying amounts and tax bases of assets and liabilities give rise to deferred tax assets and liabilities as of December 31, 2004 and 2003, respectively:

	Year ended December 31, 2004	Year ended December 31, 2003
	-----	-----
Deferred tax assets - long-term		
Net operating loss carryforwards	\$ 2,669,000	\$ 2,900,000
Deferred tax liabilities - long-term		
Statutory depreciation differences	(690,000)	(250,000)
	-----	-----
	1,979,000	2,650,000
Less valuation allowance	(1,979,000)	(2,650,000)
	-----	-----
Net Deferred Tax Asset	\$ -	\$ -
	=====	=====

During the years ended December 31, 2004 and 2003, respectively, the valuation allowance increased (decreased) by approximately \$(671,000) and \$656,000.

### Note N - Revenue Concentrations

The Company sells to both commercial and governmental customers, in both domestic and foreign markets. The following table shows the Company's gross revenue composition:

Year ended December 31, 2004		Year ended December 31, 2003	
-----		-----	
Amount	% of total	Amount	% of total
-----	-----	-----	-----

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Domestic

Commercial

Customer A	\$	-	-	\$ 524,210	24.96
Customer B		-	-	463,423	22.07
Customer C		-	-	188,546	8.98
Others		1,827,104	56,26	348,022	16.58
		1,827,104	56,26	1,524,201	72.59

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AMERICAN AMMUNITION, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

Note N - Revenue Concentrations - Continued

	Year ended December 31, 2004		Year ended December 31, 2003	
	Amount	% of total	Amount	% of total
Governmental				
Customer D	-	-	421,290	20.06
Customer E	698,976	21.52	-	-
Others	8,905	0.28	23,663	1.12
	707,881	21.80	444,953	21.18
Foreign				
Governmental				
Customer F	684,340	21.07	-	-
Others	28,043	0.87	130,710	6.23
	712,383	21.94	130,710	6.23
Totals	\$3,247,368	100.00	\$2,099,864	100.00

Note O - Selected Financial Data (Unaudited)

The following is a summary of the quarterly results of operations for the years ended December 31, 2004 and 2003, respectively.



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	Quarter ended March 31,	Quarter ended June 30,	Quarter ended September 30,	Quarter ended December 31,	Y D
-----					
Calendar 2004					
Revenues - net	\$ 281,507	\$ 568,785	\$ 861,988	\$ 1,535,088	\$
Gross profit	\$ (423,626)	\$ (676,300)	\$ 377,181	\$ (650,553)	\$
Net earnings after provision for income taxes	\$ (1,188,358)	\$ (1,155,307)	\$ 9,552	\$ (983,960)	\$
Basic and fully diluted earnings per share	\$ (0.02)	\$ (0.02)	\$ 0.00	\$ (0.01)	\$
Weighted average number of shares issued and outstanding	67,769,150	71,148,043	73,673,416	74,616,136	
Calendar 2003					
Revenues - net	\$ 608,437	\$ 289,551	\$ 317,729	\$ 769,280	\$
Gross profit	\$ (66,668)	\$ (463,653)	\$ (462,483)	\$ (254,221)	\$
Net earnings after provision for income taxes	\$ (300,355)	\$ (1,232,951)	\$ (1,200,981)	\$ (205,108)	\$
Basic and fully diluted earnings per share	\$ (0.01)	\$ (0.02)	\$ (0.02)	nil	\$
Weighted average number of shares issued and outstanding	56,638,979	59,294,402	61,683,424	66,253,535	

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