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[Table of Contents](#)

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended April 1, 2012

OR

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

For the transition period from _____ to _____

Registration number 333-171547

Colt Defense LLC Colt Finance Corp.

(Exact name of Registrant as specified in its charter)

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

32-0031950
27-1237687
(I.R.S. Employer
Identification No.)

547 New Park Avenue, West Hartford, CT
(Address of principal executive offices)

06110
(Zip Code)

(860) 232-4489
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

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

The number of shares outstanding of the Registrant's common stock as of May 1, 2012 was none.

[Table of Contents](#)**COLT DEFENSE LLC AND SUBSIDIARIES
INDEX**

	<u>Page</u>
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements (unaudited)</u>	
<u>Consolidated Balance Sheets — As of April 1, 2012 and December 31, 2011</u>	3
<u>Consolidated Statements of Operations — Three Months Ended April 1, 2012 and April 3, 2011</u>	4
<u>Consolidated Statements of Comprehensive Loss — Three Months Ended April 1, 2012 and April 3, 2011</u>	5
<u>Consolidated Statements of Changes in Cash Flows — Three Months Ended April 1, 2012 and April 3, 2011</u>	6
<u>Notes to Consolidated Financial Statements</u>	7
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	15
<u>Item 3. Quantitative and Qualitative disclosures about Market Risk</u>	20
<u>Item 4. Controls and Procedures</u>	20
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	21
<u>Item 1A. Risk Factors</u>	21
<u>Item 6. Exhibits</u>	22
<u>Signatures</u>	23

[Table of Contents](#)**PART I — FINANCIAL INFORMATION**
ITEM 1. — FINANCIAL STATEMENTS**Colt Defense LLC and Subsidiaries**
Consolidated Balance Sheets
(In thousands of dollars)
(Unaudited)

	<u>April 1, 2012</u>	<u>December 31, 2011</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 29,280	\$ 38,236
Restricted cash	1,241	1,241
Accounts receivable, net	33,035	30,575
Inventories	35,781	36,215
Other current assets	2,527	2,481
Total current assets	<u>101,864</u>	<u>108,748</u>
Property and equipment, net	21,915	22,589
Goodwill	14,902	14,713
Intangible assets with finite lives, net	6,547	6,635
Deferred financing costs	8,882	9,312
Long-term restricted cash	810	810
Other assets	1,995	2,149
Total assets	<u>\$ 156,915</u>	<u>\$ 164,956</u>
LIABILITIES AND DEFICIT		
Current liabilities:		
Capital lease obligations — current portion	\$ 825	\$ 1,148
Accounts payable	8,805	11,114
Accrued compensation and benefits	3,462	4,984
Accrued commissions	1,110	2,872
Accrued expenses	5,674	5,410
Pension and retirement obligations - current portion	890	890
Accrued interest	8,422	2,923
Customer advances and deferred income	8,913	8,804
Accrued distributions to members	—	3,343
Total current liabilities	<u>38,101</u>	<u>41,488</u>
Long-term debt, less current portion	247,280	247,186
Pension and retirement liabilities	17,452	17,953
Other long-term liabilities	1,512	1,501
Total long-term liabilities	<u>266,244</u>	<u>266,640</u>
Total liabilities	<u>304,345</u>	<u>308,128</u>
Commitments and Contingencies (Note 10)		
Deficit:		
Accumulated deficit	(137,370)	(130,769)
Accumulated other comprehensive loss	(10,060)	(12,403)
Total deficit	<u>(147,430)</u>	<u>(143,172)</u>
Total liabilities and deficit	<u>\$ 156,915</u>	<u>\$ 164,956</u>

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

[Table of Contents](#)

Colt Defense LLC and Subsidiaries
Consolidated Statements of Operations
(In thousands of dollars)
(Unaudited)

	For the Three Months Ended	
	April 1, 2012	April 3, 2011
Net sales	\$ 44,577	\$ 48,497
Cost of sales	36,270	35,425
Gross profit	8,307	13,072
Selling and commissions	2,944	3,296
Research and development	1,265	727
General and administrative	4,304	3,477
Amortization of purchased intangibles	126	136
Operating (loss) income	(332)	5,436
Interest expense	6,100	6,085
Other income, net	(238)	(29)
Non-operating expense	5,862	6,056
Loss before provision for foreign income taxes	(6,194)	(620)
Provision for foreign income taxes	416	1,139
Net loss	<u>\$ (6,610)</u>	<u>\$ (1,759)</u>

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

[Table of Contents](#)

Colt Defense LLC and Subsidiaries
Consolidated Statements of Comprehensive Loss
(In thousands of dollars)
(Unaudited)

	<u>For the Three Months Ended</u>	
	<u>April 1, 2012</u>	<u>April 3, 2011</u>
Net loss	\$ (6,610)	\$ (1,759)
Other comprehensive income, net of tax:		
Foreign currency translation adjustments	398	1,056
Change in pension and retirement benefit plans	1,945	96
Comprehensive loss	<u>\$ (4,267)</u>	<u>\$ (607)</u>

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

[Table of Contents](#)

Colt Defense LLC and Subsidiaries
Consolidated Statements of Changes in Cash Flows
(In thousands of dollars)
(Unaudited)

	For the Three Months Ended	
	April 1, 2012	April 3, 2011
Operating Activities		
Net loss	\$ (6,610)	\$ (1,759)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	1,440	1,370
Amortization of financing fees	413	363
Deferred foreign income taxes	(99)	(43)
Amortization of debt discount	94	87
Pension curtailment expense	1,527	—
Amortization of deferred income	—	(47)
Loss on sale/disposal of fixed assets	11	—
Common unit compensation expense	9	—
Changes in operating assets and liabilities:		
Accounts receivable	(2,338)	(18,620)
Inventories	579	(5,262)
Prepaid expenses and other assets	61	404
Accounts payable and accrued expenses	29	12,225
Accrued pension and retirement liabilities	(83)	(171)
Customer advances and deferred income	(45)	1,096
Other	129	47
Net cash used in operating activities:		
Continuing operations	(4,883)	(10,310)
Discontinued operations	—	(28)
Net cash used in operating activities	<u>(4,883)</u>	<u>(10,338)</u>
Investing Activities		
Purchases of property and equipment	(563)	(1,215)
Proceeds from disposal of property	66	—
Net cash used in investing activities	<u>(497)</u>	<u>(1,215)</u>
Financing Activities		
Capital lease obligation payments	(323)	(298)
Distributions paid to members	(3,343)	—
Net cash used in financing activities	<u>(3,666)</u>	<u>(298)</u>
Effect of exchange rates on cash	90	287
Change in cash and cash equivalents	(8,956)	(11,564)
Cash and cash equivalents, beginning of period	38,236	61,444
Cash and cash equivalents, end of period	<u>\$ 29,280</u>	<u>\$ 49,880</u>
Supplemental Disclosure of Cash Flow Information		
Cash paid for interest	\$ 84	\$ 63
Cash paid for foreign income taxes	1,599	572
Accrued distribution to members	—	12,889
Non-cash consideration for sale of equipment	75	—

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

[Table of Contents](#)**Notes to Consolidated Financial Statements (unaudited)**

(in thousands of dollars)

Note 1 — Basis of Presentation

The accompanying unaudited consolidated financial statements of Colt Defense LLC and Colt Finance Corp. (the “Company”, “Colt”, “we”, or “us”) have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all significant adjustments (consisting of normal recurring accruals) considered necessary for a fair statement of the financial position, results of operations and cash flows for the three months ended April 1, 2012 and April 3, 2011 have been included. The financial information included in this quarterly report on Form 10-Q should be read in conjunction with the consolidated financial statements and notes in the Annual Report on Form 10-K for the fiscal year ended December 31, 2011, which was filed with the Securities and Exchange Commission on February 24, 2012. The consolidated balance sheet dated December 31, 2011 included in this quarterly report on Form 10-Q has been derived from the audited consolidated financial statements at that time, but does not include all disclosures required by GAAP.

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated. We have reclassified certain prior period amounts to conform with our current year presentation. Operating results for the three months ended April 1, 2012 are not necessarily indicative of the results to be expected for any subsequent interim period or for the year ending December 31, 2012.

Recent Accounting Pronouncements

Presentation of Comprehensive Income — In June 2011, the Financial Accounting Standards Board (“FASB”) issued ASU 2011-05, which requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income, or in two separate but consecutive statements. This update eliminates the option to present components of other comprehensive income as part of the statement of equity, but it does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. In December 2011, FASB issued ASU 2011-12, which amends ASU 2011-05. This amendment defers the requirement to present components of reclassifications of other comprehensive income on the face of the income statement. Both standards were effective for us beginning on January 1, 2012. The adoption of these standards had no impact on our consolidated financial statements.

Intangibles — Goodwill and Other — In September 2011, FASB issued ASU 2011-08, which provides entities the option to perform a qualitative assessment in order to determine whether additional quantitative impairment testing is necessary. This amendment is effective for reporting periods beginning after December 15, 2011. This amendment does not impact the quantitative testing methodology, should it be necessary. We adopted this standard on January 1, 2012 and it had no impact on our operating results or financial position.

Fair Value Measurement — In May 2011, FASB issued an amendment to revise the wording used to describe the requirements for measuring fair value and for disclosing information about fair value measurements. For many of the requirements, the FASB does not intend for the amendments to result in a change in the application of existing fair value measurement requirements, such as specifying that the concepts of the highest and best use and valuation premise in a fair value measurement are relevant only when measuring the fair value of nonfinancial assets. Other amendments change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements such as specifying that, in the absence of a Level 1 input, a reporting entity should apply premiums or discounts when market participants would do so when pricing the asset or liability. The amendment is effective for interim and annual periods beginning after December 15, 2011. We adopted this standard on January 1, 2012 and it had no impact on our operating results or financial position.

Goodwill

The net carrying amount of goodwill may change from period to period as a result of fluctuations in exchange rates at our Canadian operation.

Prior Period Adjustments

During the first quarter of 2011, we recorded a pre-tax adjustment of \$127, related to immaterial errors in prior periods. Management has concluded based on its quantitative and qualitative analysis such amounts are not material to our operations.

[Table of Contents](#)**Note 2 — Accounts Receivable**

Accounts receivable are net of an allowance for doubtful accounts of \$0 and \$1 at April 1, 2012 and December 31, 2011, respectively.

Note 3 — Inventories

Inventories consist of:

	<u>April 1, 2012</u>	<u>December 31, 2011</u>
Materials	\$ 24,875	\$ 22,422
Work in process	7,777	8,211
Finished products	3,129	5,582
	<u>\$ 35,781</u>	<u>\$ 36,215</u>

Note 4 — Notes Payable and Long-term Debt***Credit Agreement***

On September 29, 2011, we entered into a credit agreement (the “Credit Agreement”) with Wells Fargo Capital Finance, LLC. Under the terms of the Credit Agreement, senior secured revolving loans are available up to \$50,000, inclusive of \$20,000 available for letters of credit. Revolving loans are subject to, among other things, the borrowing base, which is calculated monthly based on specified percentages of eligible accounts receivable and inventory and specified values of fixed assets. Under the Credit Agreement, our obligations are secured by a first-priority security interest in substantially all of our assets, including accounts receivable, inventory and certain other collateral. The Credit Agreement matures on September 28, 2016.

Borrowings under the Credit Agreement bear interest at a variable rate based on the London Inter-Bank Offer Rate (“LIBOR”), the Canadian Banker’s Acceptance Rate or the lender’s prime rate, as defined in the Credit Agreement, plus a spread. The interest rate spread on borrowing varies based on both the rate option selected and our quarterly average excess availability under the Credit Agreement.

The Credit Agreement limits the Company’s ability to incur additional indebtedness, make investments or certain payments, pay dividends and merge, acquire or sell assets. In addition, certain covenants would be triggered if excess availability were to fall below the specified level, including a fixed charge coverage ratio requirement. Excess availability is determined as the lesser of our borrowing base or \$50,000, reduced by outstanding obligations under the Credit Agreement and trade payables that are more than 60 days past due. The Credit Agreement contains customary events of default. In addition, if excess availability falls below \$9,000 and the fixed charge coverage ratio is less than 1.0 to 1.0, the Company would be in default under the Credit Agreement. The Company was in compliance with all covenants and restrictions and there were no borrowings or letters of credit outstanding under the Credit Agreement as of April 1, 2012.

Senior Notes

On November 10, 2009, Colt Defense LLC and Colt Finance Corp, our 100%-owned subsidiary, jointly and severally co-issued \$250,000 of unsecured senior notes (“the Senior Notes”). The Senior Notes bear interest at 8.75% and mature on November 15, 2017. Interest is payable semi-annually in arrears on May 15 and November 15, commencing on May 15, 2010. We issued the Senior Notes at a discount of \$3,522 from their principal value. This discount is being amortized as additional interest expense over the life of the indebtedness. No principal repayments are required until maturity.

The Senior Notes are not guaranteed by any of our subsidiaries and do not have any financial condition covenants that require us to maintain compliance with any financial ratios or measurements on a periodic basis. The Senior Notes do contain non-financial condition covenants that, among other things, limit our ability to incur additional indebtedness, enter into certain mergers or consolidations, incur certain liens and engage in certain transactions with our affiliates. In addition, the indenture restricts our ability to pay dividends or make other Restricted Payments (as defined in the indenture) to our members, subject to certain exceptions. Such restrictions are not expected to affect our ability to meet our cash obligations for the next 12 months. Additionally, the Senior Notes contain certain cross default provisions with other indebtedness, if such indebtedness in default aggregates to \$20,000 or more.

The outstanding loan balances at April 1, 2012 and December 31, 2011 were as follows:

[Table of Contents](#)

	<u>April 1, 2012</u>	<u>December 31, 2011</u>
Senior notes principal amount	\$ 250,000	\$ 250,000
Unamortized discount	(2,720)	(2,814)
	<u>\$ 247,280</u>	<u>\$ 247,186</u>

	<u>Three Months Ended</u>	
	<u>April 1, 2012</u>	<u>April 3, 2011</u>
Effective interest rate	9.0%	9.1%
Amortization of discount	\$ 94	\$ 87
Amortization of deferred financing costs	413	363

Note 5 - Income Taxes

As a limited liability company, we are treated as a partnership for U.S. federal and state income tax reporting purposes and therefore, are not subject to U.S. federal or state income taxes. Our taxable income (loss) is reported to our members for inclusion in their individual tax returns. Our Canadian operation files separate income tax returns in Canada. Our limited liability agreement requires that in any year in which U.S. taxable income is allocated to the members, we make distributions to members equal to 45% of the highest taxable income allocated to any one unit, to the extent our Governing Board determines that sufficient funds are available.

The provision (benefit) for foreign income taxes consists of the following:

	<u>Three Months Ended</u>	
	<u>April 1, 2012</u>	<u>April 3, 2011</u>
Current	\$ 515	\$ 1,182
Deferred	(99)	(43)
Total	<u>\$ 416</u>	<u>\$ 1,139</u>

Note 6 — Colt Defense LLC Deficit

Our authorized capitalization consists of 1,000,000 common units and 250,000 preferred units. Common units issued and outstanding as of April 1, 2012 and December 31, 2011 were 132,174. No preferred units have been issued.

In March 2012, we paid our members a tax distribution of \$3,343, which had been accrued in December 2011.

Note 7 — Common Unit Compensation

On March 1, 2012, the Governing Board approved the Colt Defense Long Term Incentive Plan (the "Plan"). The purpose of the Plan is to advance the interests of Colt Defense and its equity holders by providing a means to attract, retain and motivate key employees, advisors and members of the Governing Board. Awards under the Plan may consist of options, restricted units, restricted phantom units, performance units or other unit-based awards. A total of 18,878 common units have been reserved for issuance in connection with awards under the Plan.

[Table of Contents](#)

Under the Plan, the exercise price of option awards is set at the grant date and may not be less than the fair market value per unit on that date. The term of each option is ten years from the grant date. The vesting periods, which vary by grant, may be time based, performance based or a combination thereof. Compensation expense equal to the grant date fair value is generally recognized over the period during which the employee is required to provide service in exchange for the award or as the performance obligation is met. Fair value was estimated on the date of grant using the Black-Scholes valuation method.

In March 2012, options were granted for 11,325 common units at a weighted-average exercise price of \$100.00 (not in thousands). For the three months ended April 1, 2012, we recorded \$9 of common unit compensation expense in general and administrative expense in our Consolidated Statements of Operations. We did not have any common unit compensation expense in the first quarter of 2011.

Note 8 — Pension, Savings and Postretirement Benefits

We have two noncontributory, domestic defined benefit pension plans that cover substantially all eligible salaried and hourly U.S. employees.

On March 31, 2012, we agreed to a new two-year collective bargaining agreement with Local 376 of the United Auto Workers (“Union”). Under the terms of the new contract, the accrual of benefits for employees participating in our bargaining unit pension plan will freeze effective December 31, 2012. All new bargaining unit employees hired after April 1, 2012 are no longer eligible to participate in the bargaining unit defined benefit plan. Instead, they will be eligible for our defined contribution 401k retirement plan.

Pension benefits under the salaried defined benefit plans have been frozen since 2009. Accordingly, participants retain the pension benefits already accrued, however no additional benefits will accrue.

The components of cost recognized in our Consolidated Statements of Operations for our pension plans are as follows:

	Three Months Ended	
	April 1, 2012	April 3, 2011
Service cost	\$ 106	\$ 72
Interest cost	269	271
Expected return on assets	(393)	(387)
Amortization of unrecognized prior service costs	42	42
Curtailement of bargaining unit plan	1,527	—
Amortization of unrecognized loss	220	123
Net periodic cost	<u>\$ 1,771</u>	<u>\$ 121</u>

We also provide certain postretirement health care coverage to retired U.S. employees who were subject to our collective bargaining agreement when they were employees. The cost of these postretirement benefits is determined actuarially and is recognized in our consolidated financial statements during the employees’ active working career.

The components of cost recognized in our Consolidated Statements of Operations for our post-retirement health plan are as follows:

[Table of Contents](#)

	Three Months Ended	
	April 1, 2012	April 3, 2011
Service cost	\$ 63	\$ 64
Interest cost	135	167
Amortization of unrecognized prior service costs	(58)	(71)
Amortization of unrecognized loss	19	2
Net periodic cost	<u>\$ 159</u>	<u>\$ 162</u>

Per our collective bargaining agreement, we cap our monthly contribution to the cost of providing retiree health care benefits at approximately \$250 (not in thousands) per employee. For the year ended December 31, 2011, the cost per month was \$186 (not in thousands) per employee. For the quarter ended April 1, 2012, the cost per month was \$184 (not in thousands) per employee.

Note 9- Transactions with Related Parties

We have a financial advisory agreement with Sciens Management LLC, an affiliate of Sciens Capital Management LLC. Under the terms of the agreement, we also reimburse the affiliate for expenses incurred in connection with the financial advisory services provided. The cost for these advisory services and the expenses are recorded within general and administrative expenses.

We have a license agreement (the "License") with New Colt Holding Corp ("NCHC"), an affiliate, for the use of certain Colt trademarks. Under the terms of the License, we received a 20-year paid-up license for the use of the Colt trademarks, which expires December 31, 2023. Thereafter, the License may be extended for successive five-year periods. Consideration for the License included the transfer to NCHC's wholly owned subsidiary, Colt's Manufacturing Company LLC ("Colt's Manufacturing"), of the Colt Match Target® rifle line of business, inventories of \$18 and cash of \$2,000. The total transferred of \$2,018 is recorded in other assets and is being amortized over 20 years. This intangible had an unamortized balance of \$1,185 at April 1, 2012 and \$1,210 at December 31, 2011.

Effective July 1, 2007, we entered into a service agreement with Colt's Manufacturing, an affiliated entity, which provides for remuneration for certain factory, accounting, data processing and management services provided by us to Colt's Manufacturing. Since January 1, 2009, the annual fee has been \$430. In accordance with the terms of this agreement, we have provided Colt's Manufacturing the required six-months notice that we do not wish to extend the service agreement, under existing terms, beyond the end of its term on June 30, 2012.

In May 2011, we signed a memorandum of understanding ("MOU") with Colt's Manufacturing to jointly coordinate the marketing and sales of rifles in the commercial market. For additional information about sales and accounts receivable under this MOU, see Note 12 Segment Information and Note 13 Concentration of Risk in this Form 10-Q. We also lease our West Hartford facility from an affiliate and we sublease a portion of our facility to Colt's Manufacturing. In addition, Colt Security LLC ("Security"), a wholly owned subsidiary of Employee Plan Holding Corp., provides security guard services to us.

Note 10 - Commitments and Contingencies

A summary of standby letters of credit issued principally in connection with performance and warranty bonds established for the benefit of certain international customers is as follows:

	April 1, 2012	December 31, 2011
Standby letters of credit secured by restricted cash	\$ 1,683	\$ 1,660
Guarantees of standby letters of credit established by a sales agent on behalf of Colt	804	804

At April 1, 2012 and December 31, 2011, we had unconditional purchase obligations related to capital expenditures for machinery and equipment of \$1,713 and \$2,102, respectively.

We also had certain Industrial Cooperation Agreements, which stipulate our commitments to provide offsetting business to certain countries that have purchased our products. We generally settle our offset purchase commitments under Industrial Cooperation Agreements through on-going business and/or cooperating with other contractors on their spending during the related period. Additionally, we identify future purchases and other satisfaction plans for the remainder of the offset purchase commitment period and should there be a projected net purchase commitment after such consideration, we accrue the estimated cost to settle the offset purchase commitment.

[Table of Contents](#)

Our remaining gross offset purchase commitment is the total amount of offset purchase commitments reduced for claims submitted and approved by the governing agencies. At April 1, 2012 and December 31, 2011, our remaining gross offset purchase commitments totaled \$59,225 and \$58,466, respectively. We have evaluated our settlement of our remaining gross offset purchase commitments through probable planned spending and other probable satisfaction plans to determine our net offset purchase commitment. We have accrued \$1,633 and \$1,563 as of April 1, 2012 and December 31, 2011, respectively, based on our estimated cost of settling the remaining net offset purchase commitment.

We are involved in various legal claims and disputes in the ordinary course of our business. As such, the Company accrues for such liabilities when it is both (i) probable that a loss has occurred and (ii) the amount of the loss can be reasonably estimated in accordance with ASC 450, Contingencies. The Company evaluates, on a quarterly basis, developments affecting various legal claims and disputes that could cause an increase or decrease in the amount of the liability that has been previously accrued. During the first quarter of 2012, we accrued \$0.7 million with respect to a potential settlement of a dispute. In determination of this accrual, the Company has estimated a range of potential liability. It is possible that the Company could incur losses in excess of any amounts accrued. While management does not anticipate any such loss would have a material adverse impact on the Company's consolidated financial position; however, it is possible that the final outcome could have a material impact on the Company's results of operations or cash flows in any given period.

Note 11 —Segment Information

Our small arms weapons systems segment represents our core business, as substantially all of our operations are conducted through this segment. Our small arms weapons systems segment consists of two operating segments which have similar economic characteristics and have been aggregated into the Company's only reportable segment. The small arms weapons systems segment designs, develops and manufactures small arms weapons systems for military and law enforcement personnel both domestically and internationally. In addition, we sell rifles and carbines to our affiliate, Colt's Manufacturing, which resells them into the commercial market.

Adjusted EBITDA consists of income (loss) before interest, income taxes, depreciation and amortization and other expenses as noted below. Management uses Adjusted EBITDA to evaluate the financial performance of and make operating decisions for the small arms weapons systems segment. See the footnotes that follow the reconciliation tables below for additional information regarding the adjustments made to arrive at Adjusted EBITDA of the small arms weapons systems segment.

The following table represents a reconciliation of adjusted EBITDA to net loss:

Statement of Operations Data:	April 1, 2012	April 3, 2011
Adjusted EBITDA	\$ 2,743	\$ 6,939
Provision for foreign income taxes	(416)	(1,139)
Depreciation and amortization (i)	(1,440)	(1,370)
Interest expense, net	(6,100)	(6,085)
Sciens fees and expenses (ii)	(108)	(133)
Pension curtailment expense (iii)	(1,527)	—
Other income, net (iv)	238	29
Net loss	<u>\$ (6,610)</u>	<u>\$ (1,759)</u>

- (i) Includes depreciation and amortization of intangible assets.
- (ii) Includes fees and expenses pursuant to our financial advisory agreement with Sciens Management LLC, an affiliate of Sciens Capital Management.
- (iii) Noncash expense associated with the curtailment of our bargaining unit pension plan
- (iv) Includes expenses incurred in connection with transaction costs incurred in connection with our contemplated merger and acquisition activities, foreign currency exchange gains or losses, service income from an affiliate and other less significant charges not related to on-going operations.

Geographical Information

Geographic external revenues are attributed to the geographic regions based on the customer's location of origin. Our reported net sales in the United States include revenues that arise from sales to the U.S. Government under its Foreign Military Sales program, which involve product that is resold by the U.S. Government to foreign governments and that we generally ship directly to the foreign government.

The table below presents net sales for specific geographic regions:

	Three Months Ended	
	April 1, 2012	April 3, 2011
United States	\$ 13,239	\$ 20,694
Canada	11,573	6,323
Asia/Pacific	15,207	7,930
Europe	2,344	11,993
Middle East/Africa	1,573	7
Latin America/Caribbean	641	1,550
	<u>\$ 44,577</u>	<u>\$ 48,497</u>

[Table of Contents](#)*Major Customer Information*

For the three months ended April 1, 2012, sales to one domestic customer, Colt's Manufacturing, represented 17% of net sales. For the three months ended April 1, 2011, sales to one domestic customer, the U.S. Government, represented 36% of net sales.

For the three months ended April 1, 2012, two direct foreign customers accounted for 34% and 20% of net sales, respectively. For the three months ended April 3, 2011, two direct foreign customers accounted for 17% and 15% of net sales, respectively.

Note 12 - Concentration of risk*Accounts Receivable*

Financial instruments, which potentially subject us to concentration of credit risk, consist primarily of accounts receivable. At April 1, 2012, the largest individual trade receivable balances accounted for 45%, 16% and 12% of total receivables, respectively. At December 31, 2011, the largest individual trade receivable balances accounted for 53%, 15% and 10% of total accounts receivables, respectively.

Labor

The Union represents approximately 61% of our U.S. workforce. On March 31, 2012, we and the Union agreed to a new, two-year collective bargaining agreement.

Note 13 — Fair Value of Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses and other current assets and liabilities approximate their fair value due to their short maturities. The carrying value of our long-term debt of \$247,280 and \$247,186 at April 1, 2012 and December 31, 2011, respectively, was recorded at amortized cost. The estimated fair value of long-term debt of approximately \$176,400 and \$172,500 at April 1, 2012 and December 31, 2011, respectively, was based on quoted market prices, which are Level 1 inputs.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The inputs used to measure fair value fall into the following hierarchy:

Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2: Unadjusted quoted prices in active markets for similar assets or liabilities, or unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability.

Level 3: Unobservable inputs for the asset or liability.

As of April 1, 2012 and December 31, 2011, we did not have any financial assets and liabilities reported at fair value and measured on a recurring basis or any significant nonfinancial assets or nonfinancial liabilities. Therefore, we did not have any transfers of assets and liabilities between Level 1 and Level 2 of the fair value measurement hierarchy during the three months ended April 1, 2012.

[Table of Contents](#)**Note 14 — Accumulated Other Comprehensive Loss**

The components of accumulated other comprehensive loss were as follows:

	Unrecognized Prior Service Cost	Unrecognized Loss	Foreign Currency Translation	Total
Balance, December 31, 2010	\$ (201)	\$ (8,898)	\$ 2,659	\$ (6,440)
Pension liability	43	123	—	166
Change in post-retirement health liability	(71)	1	—	(70)
Currency translation	—	—	1,056	1,056
Balance, April 3, 2011	<u>(229)</u>	<u>(8,774)</u>	<u>3,715</u>	<u>(5,288)</u>
Balance, December 31, 2011	(261)	(14,357)	2,215	(12,403)
Pension liability	619	1,365	—	1,984
Change in post-retirement health liability	(58)	19	—	(39)
Currency translation	—	—	398	398
Balance, April 1, 2012	<u>\$ 300</u>	<u>\$ (12,973)</u>	<u>\$ 2,613</u>	<u>\$ (10,060)</u>

[Table of Contents](#)**ITEM 2. — MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

This Form 10-Q, including the documents that we incorporate by reference, contain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, that are subject to the “safe harbor” created by those sections. Any statements about our expectations, beliefs, plans, objectives, assumptions or future events or our future financial performance and/or operating performance are not statements of historical fact and reflect only our current expectations regarding these matters. These statements are often, but not always, made through the use of words such as “may,” “will,” “expect,” “anticipate,” “believe,” “intend,” “predict,” “potential,” “estimate,” “plan” or variations of these words or similar expressions. These statements inherently involve a wide range of known and unknown uncertainties. Our actual actions and results may differ materially from what is expressed or implied by these statements. Factors that could cause such a difference include, but are not limited to, those set forth as “Risk Factors” under Section 1A herein and in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011, which was filed with the Securities and Exchange Commission on February 24, 2012. Given these factors, you should not rely on forward-looking statements, assume that past financial performance will be a reliable indicator of future performance nor use historical trends to anticipate results or trends in future periods. We expressly disclaim any obligation or intention to provide updates to the forward-looking statements and estimates and assumptions associated with them.

Certain monetary amounts, percentages and other figures included in this section have been subject to rounding adjustments. Accordingly, figures shown as totals in certain tables may not be the arithmetic aggregation of the figures that precede them and figures expressed as percentages in the text may not total 100% or, as applicable, when aggregated may not be the arithmetic aggregation of the percentages that precede them.

Overview of Our Business

We are one of the world’s leading designers, developers and manufacturers of small arms weapons systems for individual soldiers and law enforcement personnel. We have supplied small arms weapons systems to more than 80 countries by expanding our portfolio of products and services to meet evolving military and law enforcement requirements around the world. Our products have proven themselves under the most severe battle conditions, including the jungles of Vietnam, the deserts of the Middle East, the urban centers of Iraq and the mountains of Afghanistan. We also modify our rifles and carbines for civilian use and sell them to our affiliate, Colt’s Manufacturing, which resells them into the commercial market.

Our development and sales of M4 carbines and the 50 years of sales of M16 rifles, have resulted in a global installed base of more than 7 million M16/M4 small arms weapons systems. We are also the Canadian military’s exclusive supplier of the C8 carbine and C7 rifle, and a supplier of other small arms weapons systems to U.S., Canadian and international law enforcement agencies. Our expertise in designing and manufacturing small arms weapons systems enables us to integrate new technologies and features into our large installed base, develop international co-production opportunities and capitalize on our experience building to stringent military standards to make commercial rifles and carbines of exceptional reliability, performance and accuracy. Based upon the expiration in 2010 of our M4 IDIQ contract and the general decline in U.S. Government rifle procurement patterns, we have placed renewed emphasis on the International and Commercial/LE markets. As a result, we have experienced strong year over year sales growth in both of these markets in the first quarter of 2012. Although the U.S. Government has recently awarded to another manufacturer a contract to produce the Colt M4, Colt, as the owner of the M4 Technical Data Package, maintains its position as the sole provider of U.S. Government-grade M4 carbines to the international market and to domestic law enforcement and commercial markets.

Our facilities in West Hartford, Connecticut and Kitchener, Ontario, Canada manufacture and sell military and law enforcement rifles, carbines, machine guns and related products and services world-wide as well as commercial model products in the United States. On March 31, 2012, we agreed to a new, two-year collective bargaining agreement with the Union that represents approximately 250 employees at our West Hartford facility.

Results of Operations

The following table sets forth our results of operations in dollars and as a percentage of total net sales for the periods presented (dollars in thousands):

	Three Months Ended			
	April 1, 2012	%	April 3, 2011	%
Statement of Operations Data:				
Net sales	\$ 44,577	100.0%	\$ 48,497	100.0%
Cost of sales	36,270	81.4	35,425	73.0
Gross profit	8,307	18.6	13,072	27.0
Selling and commissions	2,944	6.6	3,296	6.8
Research and development	1,265	2.8	727	1.5
General and administrative	4,304	9.7	3,477	7.2
Amortization of purchased intangibles	126	0.3	136	0.3
	8,639	19.4	7,636	15.7
Operating (loss) income	(332)	(0.7)	5,436	11.2
Interest expense	6,100	13.7	6,085	12.5
Other income, net	(238)	(0.5)	(29)	(0.1)
	5,862	13.2	6,056	12.5
Loss before provision for foreign income taxes	(6,194)	(13.9)	(620)	(1.3)
Provision for foreign income taxes	416	0.9	1,139	2.3
Net loss	\$ (6,610)	(14.8)%	\$ (1,759)	(3.6)%

[Table of Contents](#)**Three Months Ended April 1, 2012 Compared to the Three Months Ended April 3, 2011***Net Sales*

The following table shows net sales for the three months ended April 1, 2012 and April 3, 2011, respectively by product category (dollars in thousands):

	Three Months Ended		
	April 1, 2012	April 3, 2011	% Change
Weapons systems	\$ 27,944	\$ 30,526	(8.5)%
Spares / other	16,633	17,971	(7.4)%
Total	\$ 44,577	\$ 48,497	(8.1)%

Net sales for the three months ended April 1, 2012 were \$44.6 million, a decrease of \$3.9 million, or 8.1%, from \$48.5 million in the comparable prior year period.

Weapon system sales declined by \$2.6 million in the first three months of 2012 compared to the same period in 2011. Contributing to this decline was a \$12.9 million decrease in sales to the U.S. Government from the comparable period in 2011. This decline was partially mitigated by a \$7.6 million increase in Commercial/LE sales and a \$2.7 million increase in international weapon systems sales as a direct result of our strategy to diversify our sales base.

Spares/other sales decreased \$1.3 million from \$18.0 million in the first quarter of 2011 to \$16.6 million in the first quarter of 2012. The decrease was mainly due to reduced sales of M249 spare barrels to the U.S. Government.

Cost of Sales/Gross Profit

(dollars in thousands)	Three Months Ended	
	April 1, 2012	April 3, 2011
Net sales	\$ 44,577	\$ 48,497
Cost of sales	36,270	35,425
Gross profit	<u>\$ 8,307</u>	<u>\$ 13,072</u>
Gross profit as a percentage of sales	18.6%	27.0%

Our cost of sales consists of direct labor and benefits, materials and subcontractor costs and manufacturing overhead, including depreciation and amortization, utilities cost, and maintenance and repairs. Gross margin for the three months ended April 1, 2012 decreased to 18.6% from 27.0% for the three months ended April 3, 2011. In the first quarter of 2012, cost of sales included \$1.5 million of expense related to the curtailment of our bargaining unit pension plan. This non-recurring expense decreased our gross margin for the quarter by 3.7%. In the first quarter of 2012, we also had higher overhead expenses compared to the same period in 2011, primarily due to increased compensation and benefits related to an increase in our workforce and higher tooling and ammunition expenses related to new products.

[Table of Contents](#)*Selling and Commissions Expense*

(dollars in thousands)	Three Months Ended	
	April 1, 2012	April 3, 2011
Selling and commissions	\$ 2,944	\$ 3,296
Selling and commissions as a percentage of sales	6.6%	6.8%

Selling expense consists primarily of compensation, advertising, promotions, travel, trade shows, consulting fees and marketing materials. In addition, we pay commissions to independent foreign sales representatives on most foreign direct sales and to domestic distributors on most Commercial/LE sales, which generally are a percentage of the selling price. For the three months ended April 1, 2012, selling and commission expenses decreased by \$0.4 million compared to the same period in 2011. The decrease was primarily due to \$1.2 million of lower commission expense as a result of lower commissionable direct foreign sales in 2012. The decrease in commissions was partially offset by a \$0.8 million increase primarily in consulting, compensation and travel expenses to support our sales effort in the international and Commercial/LE markets.

Research and Development

(dollars in thousands)	Three Months Ended	
	April 1, 2012	April 3, 2011
Research and development	\$ 1,265	\$ 727
Research and development as a percentage of sales	2.8%	1.5%

Research and development expenses consist primarily of compensation and benefit expenses and experimental work materials for our employees who are responsible for the development and enhancement of new and existing products. Research and development increased by \$0.5 million during the first three months of 2012 as compared to the first three months of 2011. The increase was mainly due to product development efforts related to competitive bids as well as ongoing product improvement initiatives.

General and Administrative Expense

(dollars in thousands)	Three Months Ended	
	April 1, 2012	April 3, 2011
General and administrative expense	\$ 4,304	\$ 3,477
General and administrative expense as a percentage of sales	9.7%	7.2%

General and administrative expense consists of compensation and benefits expense, fees for professional services and other general office administration expenses. These costs do not change proportionately with changes in sales. During the three months ended April 1, 2012, general and administrative costs increased by \$0.8 million over the comparable three months of 2011. This year over year increase was mainly driven by a \$0.7 million accrual for the potential settlement of a dispute.

Interest Expense

Our interest expense for the three months ended April 1, 2012 and April 3, 2011 was \$6.1 million.

Other Income, net

For the three months ended April 1, 2012, we had other income of \$0.2 million compared to other income of \$29 thousand for the three months ended April 3, 2011. Foreign exchange gains and service income from our affiliate, Colt's Manufacturing were largely unchanged year over year. The increase in other income, net was primarily attributable to lower costs related to potential acquisitions in 2012.

Income Taxes

As a limited liability company, we are treated as a partnership for U.S. federal and state income tax purposes and therefore, we are not subject to U.S. federal or state income taxes. Our taxable income (loss) was reported to our members for inclusion in their individual tax returns. The income tax that we incurred results from Canadian federal and provisional income taxes as well as withholding tax required on the royalty and interest income received from our Canadian subsidiary. For the first quarter of 2012, we had foreign income tax expense of \$0.4 million compared to \$1.1 million for the first quarter of 2011.

[Table of Contents](#)**Liquidity and Capital Resources**

Our primary liquidity requirements are for debt service, working capital and capital expenditures. We have historically funded these requirements through internally-generated operating cash flow. In order to support the growth in our working capital requirements related to our expanding international business, on September 29, 2011, we entered into a Credit Agreement with Wells Fargo Capital Finance, LLC. Under the terms of the Credit Agreement, senior secured revolving loans are available up to \$50.0 million, inclusive of \$20.0 million available for letters of credit. Revolving loans are subject to, among other things, the borrowing base, which is calculated monthly based on specified percentages of eligible accounts receivable and inventory and specified values of fixed assets. Under the Credit Agreement, our obligations are secured by a first-priority security interest in substantially all of our assets, including accounts receivable, inventory and certain other collateral. The Credit Agreement matures on September 28, 2016.

Borrowings under the Credit Agreement bear interest at a variable rate based on the London Inter-Bank Offer Rate ("LIBOR"), the Canadian Banker's Acceptance Rate or the lender's prime rate, as defined in the Credit Agreement, plus a spread. The interest rate spread on borrowing varies based on both the rate option selected and our quarterly average excess availability under the Credit Agreement.

The Credit Agreement limits our ability to incur additional indebtedness, make investments or certain payments, pay dividends and merge, acquire or sell assets. In addition, certain covenants would be triggered if excess availability were to fall below the specified level, including a fixed charge coverage ratio requirement. Excess availability is determined as the lesser of our borrowing base or \$50,000, reduced by outstanding obligations under the Credit Agreement and trade payables that are more than 60 days past due. The Credit Agreement contains customary events of default. In addition, if excess availability falls below \$9,000 and the fixed charge coverage ratio is less than 1.0 to 1.0, the Company would be in default under the Credit Agreement. We were in compliance with all covenants and restrictions and there were no borrowings or letters of credit outstanding under the Credit Agreement as of April 1, 2012.

On November 10, 2009, Colt Defense LLC and Colt Finance Corp, our 100%-owned finance subsidiary, jointly and severally co-issued \$250,000 of unsecured senior notes. The Senior Notes bear interest at 8.75% and mature November 15, 2017. Interest is payable semi-annually in arrears on May 15 and November 15, commencing on May 15, 2010. We issued the Senior Notes at a discount of \$3,522 from their principal value. This discount is being amortized as additional interest expense over the life of the indebtedness. No principal repayments are required until maturity.

The Senior Notes are not guaranteed by any of our subsidiaries and do not have any financial condition covenants that require us to maintain compliance with any financial ratios or measurements on a periodic basis. The Senior Notes do contain non-financial condition covenants that, among other things, limit our ability to incur additional indebtedness, enter into certain mergers or consolidations, incur certain liens and engage in certain transactions with our affiliates. In addition, the indenture restricts our ability to pay dividends or make other Restricted Payments (as defined in the indenture) to our members, subject to certain exceptions. Such restrictions are not expected to affect our ability to meet our cash obligations for the next 12 months. Additionally, the Senior Notes contain certain cross default provisions with other indebtedness if such indebtedness in default aggregates to \$20,000 or more.

Our cash used in or generated from operating activities is generally a reflection of our operating results adjusted for non-cash charges or credits such as depreciation and amortization and changes in working capital including accounts receivable and our investment in inventory. Historically, tax distributions to our members have been made in amounts equal to 45% of our taxable income, as defined, for the applicable period. Our Governing Board may also declare other distributions to our members from time to time. In addition, our cash requirements and liquidity could be impacted by potential acquisitions.

Changes in accounts receivable and inventory can cause significant fluctuations in our cash flow from operations. U.S. Government receivables, which have historically constituted the majority of our accounts receivable, are generally collected within 20 days. Payment terms for international orders are negotiated individually with each customer. As a result, international receivables, a growing portion of our receivable base, tend to experience a longer collection cycle. Commercial/LE receivables, which grew significantly in the first quarter on 2012, tend to be collected within 30-60 days. To date, we have not experienced any significant receivable losses.

Our renewed emphasis on the international and Commercial/LE markets have also caused increased fluctuations and an overall increase in our inventory levels. Certain large international orders tend to ship upon completion of large production runs, which can cause greater fluctuations in our inventory levels. In addition, we need to maintain higher inventory levels to support our expanded product lines.

[Table of Contents](#)

At April 1, 2012, we had cash and cash equivalents totaling \$29.3 million. We believe that our existing cash balances and forecasted operating cash flows are sufficient to meet our obligations for the next twelve months. We are not aware of any significant events or conditions that are likely to have a material impact on our liquidity.

Cash Flows

The following table sets forth our consolidated cash flows for the three month ended April 1, 2012 and April 3, 2011, respectively (\$ in thousands):

	Three Months Ended	
	April 1, 2012	April 3, 2011
Cash used in operating activities	\$ (4,883)	\$ (10,338)
Cash used in investing activities	(497)	(1,215)
Cash used in financing activities	(3,666)	(298)

Cash Flows Provided by Operating Activities

Net cash used by operating activities for the three months ended April 1, 2012 was \$4.9 million, compared to net cash used by operations of \$10.3 million for the three months ended April 3, 2011. While our net loss was larger in the first quarter of 2012, it was more than offset by significantly higher funding requirements for our operating assets and liabilities in the first quarter of 2011.

During the first three months of 2012, we used \$1.7 million of cash to fund changes in operating assets and liabilities as compared to \$10.3 million used to fund changes in operating assets and liabilities during the first three months of 2011. As we transitioned to a more diverse sales base in 2011, we needed to build more working capital to support our expanding international sales, which tend to have longer production and collection cycles. While we continued to build working capital to support growing Commercial/LE sales in 2012, the rate of working capital growth has slowed compared to the prior year.

Cash Flows Used in Investing Activities

Net cash used in investing activities for both periods presented were principally for capital expenditures. These capital expenditures reflect our ongoing initiative to expand our manufacturing capabilities, upgrade our machinery and equipment and improve our overall manufacturing efficiency. We expect our full-year capital expenditures for 2012 to be approximately \$4.0 — \$6.0 million.

Capital expenditures for the three months ended April 1, 2012 were \$0.6 million compared to \$1.2 million for the three months ended April 3, 2011. In both years, capital expenditures were primarily for new product production and plant modernization.

Cash Flows Used in Financing Activities

In 2012, net cash used in financing activities was primarily to fund a \$3.3 million distribution to our members. In the first three months of 2012 and 2011, we also used \$0.3 million to make payments on our capitalized leases.

Backlog

Because a substantial portion of our business is of a build-to-order nature, we generally have a significant backlog of orders to be shipped. Our backlog increased by 20.1% from \$176.7 million at December 31, 2011 to \$212.3 million at April 1, 2012, primarily due to strong Commercial/LE bookings in the first quarter. We expect approximately 81% of our backlog of orders as of April 1, 2012 to be shipped over the next twelve months.

Recent Issued Accounting Standards

Presentation of Comprehensive Income — In June 2011, the Financial Accounting Standards Board (“FASB”) issued ASU 2011-05, which requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income, or in two separate but consecutive statements. This update eliminates the option to present components of other comprehensive income as part of the statement of equity, but it does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. In December 2011, FASB issued ASU 2011-12, which amends ASU 2011-05. This amendment defers the requirement to present components of reclassifications of other comprehensive income on the face of the income statement. Both standards were effective for us beginning on January 1, 2012. The adoption of these standards had no impact on our consolidated financial statements.

[Table of Contents](#)

Intangibles — Goodwill and Other — In September 2011, FASB issued ASU 2011-08, which provides entities the option to perform a qualitative assessment in order to determine whether additional quantitative impairment testing is necessary. This amendment is effective for reporting periods beginning after December 15, 2011, but early adoption is permitted. This amendment does not impact the quantitative testing methodology, should it be necessary. The adoption of this standard had no impact on our consolidated financial statements.

Fair Value Measurement — In May 2011, FASB issued an amendment to revise the wording used to describe the requirements for measuring fair value and for disclosing information about fair value measurements. For many of the requirements, the FASB does not intend for the amendments to result in a change in the application of existing fair value measurement requirements, such as specifying that the concepts of the highest and best use and valuation premise in a fair value measurement are relevant only when measuring the fair value of nonfinancial assets. Other amendments change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements such as specifying that, in the absence of a Level 1 input, a reporting entity should apply premiums or discounts when market participants would do so when pricing the asset or liability. The amendment is effective for interim and annual periods beginning after December 15, 2011. The adoption of this standard had no impact on our consolidated financial statements.

Critical Accounting Policies and Estimates

The preparations of our financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. The Company's reaffirms the significant accounting policies as disclosed in Note 2 of the Notes to the Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011, which was filed with the Securities and Exchange Commission on February 24, 2012.

Contractual Obligations

As of April 1, 2012, there have been no material changes to our contractual obligations outside the ordinary course of our business since December 31, 2011.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exposure

We are subject to foreign currency exchange risks relating to receipts from customers, payments to suppliers and some intercompany transactions. As a matter of policy, we do not engage in currency speculation and therefore, we have no derivative financial instruments to hedge this exposure. In our Statements of Operations, we have foreign currency gains of \$0.1 million for both the three months ended April 1, 2012 and the three months ended April 3, 2011. The foreign currency amounts reported in the Statement of Operations may change materially should our international business continue to grow or if changes in the Canadian dollar or Euro versus the U.S. dollar fluctuate materially.

Interest Rate Exposures

We had no variable rate debt outstanding at April 1, 2012.

ITEM 4. CONTROLS AND PROCEDURES

Section 404 of the Sarbanes-Oxley Act requires annual management assessments of the effectiveness of our internal control over financial reporting. The Company is not currently required to comply with Section 404 but will be required to do so prior to the filing of our annual report on Form 10-K for the year ended December 31, 2012. In preparation for compliance with Section 404 and the rules promulgated thereunder, we may identify deficiencies with respect to our internal controls over financial reporting, and any such deficiencies may be material.

Our principal executive officer and principal financial officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")), as of April 1, 2012. Based on such evaluation, they have concluded that as of such date, our disclosure controls and procedures are effective and designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in applicable SEC rules and forms, and that such information is accumulated and communicated to management, including our principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure.

[Table of Contents](#)**PART II. OTHER INFORMATION****Item 1. Legal Proceedings**

We are involved in various legal claims and disputes in the ordinary course of our business. As such, the Company accrues for such liabilities when it is both (i) probable that a loss has occurred and (ii) the amount of the loss can be reasonably estimated in accordance with ASC 450, Contingencies. The Company evaluates, on a quarterly basis, developments affecting various legal claims and disputes that could cause an increase or decrease in the amount of the liability that has been previously accrued. During the first quarter of 2012, we accrued \$0.7 million with respect to a potential settlement of a dispute. In determination of this accrual, the Company has estimated a range of potential liability. It is possible that the Company could incur losses in excess of any amounts accrued. While management does not anticipate any such loss would have a material adverse impact on the Company's consolidated financial position; however, it is possible that the final outcome could have a material impact on the Company's results of operations or cash flows in any given period.

Item 1A. Risk Factors

In addition to the information set forth in this report, you should carefully review and consider the information discussed in Part I, Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2011, which could materially affect our business, financial condition or future results. These are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem immaterial also may materially adversely affect our business, financial condition or future results.

[Table of Contents](#)**Item 6. Exhibits**

The following list of exhibits includes exhibits submitted with this Form 10-Q as filed with the Securities and Exchange Commission and those incorporated by reference to other filings.

10.1	Colt Defense LLC Long Term Incentive Plan, dated as of March 1, 2012*
10.2	Second Amendment to Amended and Restated Limited Liability Agreement of Colt Defense LLC, dated as of March 1, 2012
31.1	Certification of Gerald R. Dinkel pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
31.2	Certification of Scott B. Flaherty pursuant to Section 302 of Sarbanes-Oxley Act of 2002*
31.3	Certification of Cynthia J. McNickle pursuant to Section 302 of the Sarbanes-Oxley Act of 2002*
101.INS	XBRL Instance Document**
101.SCH	XBRL Taxonomy Extension Schema Document**
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document**
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document**
101.LAB	XBRL Taxonomy Extension Label Linkbase Document**
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document**

* Filed electronically herewith

** Furnished and not filed herewith

Notes to Exhibits List:

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheets at April 1, 2012 and December 31, 2011, (ii) Consolidated Statements of Operations for the three months ended April 1, 2012 and April 3, 2011, (iii) Consolidated Statements of Comprehensive Loss for the three months ended April 1, 2012 and April 3, 2011, (iv) Consolidated Statements of Cash Flows for the three months ended April 1, 2012 and April 3, 2011 and (v) Notes to the Consolidated Financial Statements. In accordance with Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be part of any registration statement or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

[Table of Contents](#)

Signatures

Pursuant to the requirements of the Securities Act of 1934, the registrants have duly caused this report to be signed on its behalf by the undersigned, hereunto duly authorized, in West Hartford, Connecticut, on the 2nd day of May, 2012.

COLT DEFENSE LLC

COLT FINANCE CORP.

By: /s/ Scott B. Flaherty

Scott B. Flaherty

Senior Vice President and Chief Financial Officer

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**COLT DEFENSE LLC
LONG TERM INCENTIVE PLAN**

1. Purposes.

The purposes of the Colt Defense LLC Long Term Incentive Plan are to advance the interests of Colt Defense LLC and its equity holders by providing a means to attract, retain, and motivate employees, consultants, advisors and members of the Board of Managers of Colt Defense LLC upon whose judgment, initiative and efforts the continued success, growth and development of Colt Defense LLC is dependent.

2. Definitions.

For purposes of this Plan, the following terms shall be defined as set forth below:

(a) “Award” means any Option, UAR, Restricted Unit, Restricted Phantom Unit, Performance Unit or Other Unit-Based Award granted to an Eligible Person under this Plan.

(b) “Award Agreement” means any written agreement, contract, or other instrument or document evidencing an Award.

(c) “Beneficiary” means the person, persons, trust or trusts which have been designated by such Eligible Person in his or her most recent written beneficiary designation filed with the Company to receive the benefits specified under this Plan upon the death of the Eligible Person, or, if there is no designated Beneficiary or surviving designated Beneficiary, then the person, persons, trust or trusts entitled by will or the laws of descent and distribution to receive such benefits.

(d) “Board” means the Governing Board of the Company.

(e) “Code” means the Internal Revenue Code of 1986, as amended from time to time. References to any provision of the Code shall be deemed to include successor provisions thereto and regulations thereunder.

(f) “Company” means Colt Defense LLC, a Delaware limited liability company, or any successor company.

(g) “Distribution Equivalent” means a right to receive cash, Units, or other property equal in value to distributions made with respect to a specified number of Units.

(h) “Eligible Person” means (i) an employee of, or consultant or advisor to, the Company or a Participating Affiliate or (ii) a member of the Board.

(i) “Fair Market Value” means, with respect to Units or other property, the fair market value of such Units or other property determined by such methods or procedures as shall be established from time to time by the Board. If the Units are listed on any established stock exchange or a national market system, the Fair Market Value of Units on a date shall be the closing price per Unit on the date (or, if the Units were not traded on that day, the next preceding day that the Units were traded) on the principal exchange on which the Units are traded, as such prices are officially quoted on such exchange.

(j) “LLC Agreement” means the Amended and Restated Limited Liability Company Agreement of the Company dated as of June 12, 2003, as amended from time to time.

(k) “Members” means the Persons in whose name Units are registered on the members schedule of the Company and who are admitted as additional or substituted Members pursuant to the LLC Agreement, so long as they remain Members, each in its capacity as a member of the Company. Reference to a “Member” means any one of the Members.

(l) “Option” means an option to purchase Units granted to an Eligible Person under the Plan.

(m) “Other Unit-Based Award” means a right, granted under Section 10, that relates to or is valued by reference to Units.

(n) “Participant” means an Eligible Person who has been granted an Award under the Plan.

(o) “Participating Affiliate” means any entity other than the Company that is designated by the Board as a participating employer under the Plan; provided, that the Company directly or indirectly owns at least 51% of the ownership interests in such entity.

(p) “Performance Unit” means a performance unit granted under Section 9.

(q) “Person” means any individual, corporation, partnership, limited partnership, limited liability company, limited company, joint venture, trust, unincorporated or governmental organization or any agency or political subdivision thereof.

(r) “Plan” means this Colt Defense LLC Long Term Incentive Plan.

(s) “Qualified Public Offering” means an underwritten sale to the public of the Company’s equity securities pursuant to an effective registration statement filed with the Securities and Exchange Commission on Form S-1 (or any successor form)

which results in gross proceeds to the Company and/or selling stockholders of at least \$75,000,000 and in which the managing underwriter is a nationally recognized investment banking firm; provided that a Qualified Public Offering shall not include any issuance of equity securities in any merger or other business combination, and shall not include any registration of the issuance of securities to existing securityholders or employees of the Company and its subsidiaries on Form S-4 or Form S-8 (or any successor form).

(t) “Restricted Phantom Unit” means a right, granted under Section 8, to receive Units or cash at the end of a specified deferral period.

(u) “Restricted Units” means an Award of Units under Section 7 that may be subject to certain restrictions and to a risk of forfeiture.

(v) “Subsidiary” means any entity in which the Company directly or indirectly owns at least 50% of the ownership interests.

(w) “Termination of Service” means the termination of the Participant’s employment, consulting or advisory services or Board membership with the Company or its Subsidiaries, as the case may be. A Participant employed by a Subsidiary of the Company shall also be deemed to incur a Termination of Service if the Subsidiary of the Company ceases to be such a Subsidiary, and the Participant does not immediately thereafter become an employee or Board member of, or a consultant or advisor to, the Company, another Subsidiary of the Company. In the event that a Participant who is an employee of the Company or a Subsidiary becomes a Board member or a consultant or advisor to the Company or a Subsidiary upon the Participant’s termination of employment, unless otherwise determined by the Board in its sole discretion, no Termination of Service shall be deemed to occur until such time as such Participant is no longer an employee of, or consultant or advisor to, the Company or a Subsidiary or a Board member, as the case may be. If a Participant who is a Board member becomes an employee of, or a consultant or advisor to, the Company or a Subsidiary upon such Participant ceasing to be a Board member, unless otherwise determined by the Board in its sole discretion, such termination of the Participant’s Board membership shall not be treated as a Termination of Service unless and until the Participant is no longer employed by, or a consultant or advisor to, the Company or a Subsidiary, as the case may be. Temporary absences from employment because of illness, vacation or leave of absence and transfers among the Company and its Subsidiaries shall not be considered a Termination of Service.

(x) “UAR” or “Unit Appreciation Right” means the right, granted under Section 6, to be paid an amount measured by the difference between the exercise price of the right and the Fair Market Value of Units on the date of exercise of the right, with payment to be made in cash, Units, or property as specified in the Award or determined by the Board.

(y) “Units” means Common Units of the Company, which may be either voting or nonvoting in the discretion of the Board, and such other securities as may be substituted therefor pursuant to Section 4(b) hereof.

3. Administration.

(a) Authority of the Board. The Plan shall be administered by the Board, and the Board shall have full and final authority to take the following actions, in each case subject to and consistent with the provisions of the Plan, including, without limitation, Section 15(d) below:

(i) to select Eligible Persons to whom Awards may be granted;

(ii) to designate Participating Affiliates;

(iii) to determine the number of Awards to be granted, the number of Units to which an Award may relate, the terms and conditions of any Award granted under the Plan (including, but not limited to, the exercise price and any bases for adjusting such exercise price, any restriction or condition, any schedule for lapse of restrictions or conditions relating to transferability or forfeiture, exercisability, or settlement of an Award, and waiver or accelerations thereof, and waivers of performance conditions relating to an Award, based in each case on such considerations as the Board shall determine), and all other matters to be determined in connection with an Award;

(iv) to determine whether, to what extent, and under what circumstances an Award may be settled, or the exercise price of an Award may be paid, in cash, Units, other Awards, or other property, or an Award may be canceled, forfeited, exchanged, or surrendered;

(v) to determine whether, to what extent, and under what circumstances cash, Units, other Awards, or other property payable with respect to an Award will be deferred either automatically, at the election of the Board, or at the election of the Eligible Person; provided that such deferral shall be intended to be in compliance with Section 409A of the Code;

(vi) to prescribe the form of each Award Agreement, which need not be identical for each Eligible Person;

(vii) to adopt, amend, suspend, waive, and rescind such rules and regulations and appoint such agents as the Board may deem necessary or advisable to administer the Plan; provided that no such rules or regulations shall, without the consent of an affected Participant, materially and adversely affect the rights of such Participant under any Award granted to the Participant prior to the adoption of the rules or regulations;

(viii) to correct any defect or supply any omission or reconcile any inconsistency in the Plan and to construe and interpret the Plan and any Award, rules and regulations, Award Agreement, or other instrument hereunder;

(ix) to accelerate the exercisability or vesting of all or any portion of any Award or to extend the period during which an Award is exercisable;

(x) to determine whether Units subject to an Award will be voting or nonvoting Units;

(xi) to determine the Fair Market Value of Units and other property; and

(xii) to make all other decisions and determinations as may be required under the terms of the Plan or as the Board may deem necessary or advisable for the administration of the Plan.

(b) Manner of Exercise of Board Authority. The Board shall have sole discretion in exercising its authority under the Plan. Any action of the Board with respect to the Plan shall be final, conclusive, and binding on all persons, including the Company, Participating Affiliates, Eligible Persons, and any person claiming any rights under the Plan from or through any Eligible Person. The express grant of any specific power to the Board, and the taking of any action by the Board, shall not be construed as limiting any power or authority of the Board. The Board may delegate to a subcommittee of the Board or to officers or managers of the Company or any Participating Affiliate the authority, subject to such terms as the Board shall determine, to perform administrative functions and to perform such other functions as the Board may determine, to the extent permitted under applicable law.

(c) Limitation of Liability. Each member of the Board shall be entitled to, in good faith, rely or act upon any report or other information furnished to him or her by any manager, officer, director, partner, Member or employee of the Company or any Participating Affiliate, the Company's independent certified public accountants, or other professional retained by the Company to assist in the administration of the Plan. No member of the Board, nor any manager, officer, director, partner, Member or employee of the Company acting on behalf of the Board, shall be personally liable for any action, determination, or interpretation taken or made in good faith with respect to the Plan, and all members of the Board and any officer or employee of the Company acting on their behalf shall, to the extent permitted by law, be fully indemnified and protected by the Company with respect to any such action, determination, or interpretation.

(d) Limitation on Board's Authority under 409A. Anything in this Plan to the contrary notwithstanding, the Board's authority to modify outstanding Awards shall be limited to the extent necessary so that the existence of such authority does not (i) cause an Award that is not otherwise deferred compensation subject to Section 409A of

the Code to become deferred compensation subject to Section 409A of the Code or (ii) cause an Award that is otherwise deferred compensation subject to Section 409A of the Code to fail to meet the requirements prescribed by Section 409A of the Code.

4. Units Subject to the Plan.

(a) Subject to adjustment as provided in Section 4(b) hereof, the total number of Units reserved for issuance in connection with Awards under the Plan, shall be 18,878. No Award may be granted if the number of Units to which such Award relates, when added to the number of Units previously issued under the Plan, exceeds the number of Units reserved under the preceding sentence. If any Awards are forfeited, canceled, terminated or exchanged, any Units counted against the number of Units reserved and available under the Plan with respect to such Award shall, to the extent of any such forfeiture, settlement, termination, cancellation or exchange, again be available for Awards under the Plan.

(b) In the event that the Board shall determine that any distribution in Units, recapitalization, Unit split, reverse split, reorganization, merger, consolidation, extraordinary dividend (which, for the avoidance of doubt shall not include any tax distributions made pursuant to Section 8.2 of the Amended and Restated Limited Liability Company Agreement of the Company, dated as of June 12, 2003, as amended, from time to time (including any successor agreement or arrangement)), spin-off, combination, repurchase, or Unit exchange, or other similar transaction or event, affects the Units such that an adjustment is appropriate in order to prevent dilution or enlargement of the rights of Eligible Persons under the Plan, then the Board shall, in such manner as it deems equitable, adjust any or all of (i) the number and kind of units or shares which may thereafter be issued under the Plan, (ii) the number and kind of units, shares, other securities or other consideration issued or issuable in respect of outstanding Awards, and (iii) the exercise price of any Award; provided, however, that it is intended that no adjustment shall be made pursuant to this Section 4(b) that causes any Award that is not otherwise deferred compensation subject to Section 409A of the Code to become deferred compensation subject to Section 409A of the Code. In the event the Company is recapitalized, reorganized or the capital structure of the Company is otherwise modified in connection with a Qualified Public Offering, Awards granted hereunder shall be adjusted so that the equity interests subject to the Awards and the Plan will be of the same class as the equity interests which are sold to the public in the Qualified Public Offering; provided, however, that it is intended that any such modification shall be made in a manner that either (i) does not result in the Award being considered deferred compensation under Section 409A of the Code if it is intended to be exempt from Section 409A of the Code or (ii) otherwise complies with the requirements of Section 409A of the Code.

(c) Any Units distributed pursuant to an Award may consist, in whole or in part, of authorized and unissued Units or Units acquired by purchase in the open market or in private transactions.

5. Specific Terms of Options.

(a) General. Options may be granted on the terms and conditions set forth in this Section 5. In addition, the Board may impose on any Option or the exercise thereof, at the date of grant or thereafter (subject to Section 15(d)), such additional terms and conditions, not inconsistent with the provisions of the Plan, as the Board shall determine, including terms regarding forfeiture of Options or continued exercisability of Options in the event of Termination of Service of the Eligible Person.

(b) Exercise Price. The exercise price per Unit purchasable under an Option shall be determined by the Board; provided, however, that the exercise price per Unit of an Option shall not be less than the Fair Market Value of a Unit on the date of grant of the Option.

(c) Term of Option. Unless otherwise specifically provided for in an applicable Option Agreement, the term of each Option shall be ten years from the date of grant of the Option.

(d) Vesting and Exercisability. The vesting and exercisability provisions of each Option shall be as determined by the Board and set forth in the applicable Option Agreement. The applicable Option Agreement will set forth the provisions of the Option relating to the period, if any, following Termination of Service in which the Eligible Person may exercise a vested Option.

(e) Method of Exercise. The Board shall determine at the date of grant or thereafter (subject to Section 15(d)) the methods by which the exercise price may be paid or deemed to be paid, the form of such payment (including, without limitation, cash, Units or other property), and the methods by which Units will be delivered or deemed to be delivered to Participants. Participants may exercise all or any portion of their vested Options by providing notice of exercise to the Company and electing to pay the exercise price of the Option by having the Company withhold from the Units received on exercise a number of Units having a Fair Market Value equal to the exercise price.

6. UARs. The Board is authorized to grant UARs to Eligible Persons on the following terms and conditions:

(a) Right to Payment. A UAR shall confer on the Eligible Person to whom it is granted a right to receive with respect to each Unit subject thereto, upon exercise thereof, the excess of (1) the Fair Market Value of one Unit on the date of exercise over (2) the exercise price per Unit of the UAR, as determined by the Board as of the date of grant of the UAR (which shall not be less than the Fair Market Value per Unit on the date of grant of the UAR).

(b) Other Terms. The Board shall determine, at the time of grant or thereafter (subject to Section 15(d)), the time or times at which a UAR may be exercised

in whole or in part (which shall not be more than ten years after the date of grant of the UAR), the method of exercise, method of settlement, form of consideration payable in settlement, method by which Units will be delivered or deemed to be delivered to Eligible Persons, whether or not a UAR shall be in tandem with any other Award, and any other terms and conditions of any UAR.

7. Restricted Units. The Board is authorized to grant Restricted Units to Eligible Persons on the following terms and conditions:

(a) Issuance and Restrictions. Restricted Units shall be subject to such restrictions on transferability and other restrictions, if any, as the Board may impose at the date of grant or thereafter (subject to Section 15(d)), which restrictions may lapse separately or in combination at such times, under such circumstances (including, without limitation, upon achievement of performance criteria if deemed appropriate by the Board), in such installments, or otherwise, as the Board may determine. Except to the extent restricted under the Award Agreement relating to the Restricted Units, an Eligible Person granted Restricted Units shall have all of the rights of a Unit holder.

(b) Forfeiture. Except as otherwise determined by the Board, at the date of grant or thereafter (subject to Section 15(d)), upon Termination of Service during the applicable restriction period, Restricted Units that are at that time subject to restrictions shall be forfeited; provided, however, that the Board may provide, by rule or regulation or in any Award Agreement, or may determine in any individual case, that restrictions or forfeiture conditions relating to Restricted Units will be waived in whole or in part in the event of Termination of Service resulting from specified causes, and the Board may in other cases waive in whole or in part the forfeiture of Restricted Units.

(c) Certificates for Units. Restricted Units granted under this Plan may be evidenced in such manner as the Board shall determine. If certificates representing Restricted Units are registered in the name of the Eligible Person, such certificates shall bear an appropriate legend referring to the terms, conditions, and restrictions applicable to such Restricted Units, and, unless otherwise determined by the Board, the Company shall retain physical possession of the certificate and the Participant shall deliver a power to the Company, endorsed in blank, relating to the Restricted Units.

(d) Distributions. Distributions made on Restricted Units shall be either paid at the distribution date, or deferred for payment to such date, and subject to such conditions, as determined by the Board, in cash or in restricted or unrestricted Units having a Fair Market Value equal to the amount of such dividends. Unless otherwise determined by the Board, Units distributed in connection with a Unit split or distribution in Units, and other property distributed, shall be subject to restrictions and a risk of forfeiture to the same extent as the Restricted Units with respect to which such Units or other property has been distributed.

8. Restricted Phantom Units. The Board is authorized to grant Restricted Phantom Units to Eligible Persons, subject to the following terms and conditions:

(a) Award and Restrictions. Delivery of Units or cash, as the case may be, will occur upon expiration of the deferral period specified for the Restricted Phantom Units by the Board (or, if permitted by the Board, as elected by the Eligible Person). In addition, Restricted Phantom Units shall be subject to such restrictions as the Board may impose, if any (including, without limitation, the achievement of performance criteria if deemed appropriate by the Board), at the date of grant or thereafter (subject to Section 15(d)), which restrictions may lapse at the expiration of the deferral period or at earlier or later specified times, separately or in combination, in installments or otherwise, as the Board may determine.

(b) Forfeiture. Except as otherwise determined by the Board at the date of grant or thereafter (subject to Section 15(d)), upon Termination of Service during the applicable deferral period or portion thereof to which forfeiture conditions apply (as provided in the Award Agreement evidencing the Restricted Phantom Units), or upon failure to satisfy any other conditions precedent to the delivery of Units or cash to which such Restricted Phantom Units relate, all Restricted Phantom Units that are at that time subject to deferral or restriction shall be forfeited; provided, however, that the Board may provide, by rule or regulation or in any Award Agreement, or may determine in any individual case, that restrictions or forfeiture conditions relating to Restricted Phantom Units will be waived in whole or in part in the event of Termination of Service resulting from specified causes, and the Board may in other cases waive in whole or in part the forfeiture of Restricted Phantom Units.

(c) Distribution Equivalents. The Board may determine that Distribution Equivalents on the specified number of Units covered by a Restricted Phantom Unit will be (A) paid with respect to such Restricted Phantom Unit at the distribution date in cash or in restricted or unrestricted Units having a Fair Market Value equal to the amount of such distributions, or (B) deferred with respect to such Restricted Phantom Unit and the amount or value thereof automatically deemed reinvested in additional Restricted Phantom Units or other Awards, as the Board shall determine.

9. Performance Units. The Board is authorized to grant Performance Units to Eligible Persons on the following terms and conditions:

(a) Performance Period. The Board shall determine a performance period (the "Performance Period") of one or more years or other periods and shall determine the performance objectives for grants of Performance Units. Performance objectives may vary from Eligible Person to Eligible Person and shall be based upon the performance criteria as the Board may deem appropriate. The performance objectives may be determined by reference to the performance of the Company, or of a Subsidiary or affiliate, or of a division or unit of any of the foregoing. Performance Periods may

overlap and Eligible Persons may participate simultaneously with respect to Performance Units for which different Performance Periods are prescribed.

(b) Award Value. At the beginning of a Performance Period, the Board shall determine for each Eligible Person or group of Eligible Persons with respect to that Performance Period the range of number of Units, if any, which may be fixed or may vary in accordance with such performance or other criteria specified by the Board, which shall be paid to an Eligible Person as an Award if the relevant measure of Company performance for the Performance Period is met.

(c) Significant Events. If during the course of a Performance Period there shall occur significant events as determined by the Board which the Board expects to have a substantial effect on a performance objective during such period, the Board may revise such performance objective.

(d) Forfeiture. Except as otherwise determined by the Board at the date of grant or thereafter (subject to Section 15(d)), upon Termination of Service during the applicable Performance Period, Performance Units for which the Performance Period was prescribed shall be forfeited; provided, however, that the Board may provide, by rule or regulation or in any Award Agreement, or may determine in an individual case, that restrictions or forfeiture conditions relating to Performance Units will be waived in whole or in part in the event of Terminations of Service resulting from specified causes, and the Board may in other cases waive in whole or in part the forfeiture of Performance Units.

(e) Payment. Each Performance Unit may be paid in whole Units, or cash, or a combination of Units and cash either as a lump sum payment or in installments, all as the Board shall determine, at the time of grant of the Performance Unit or otherwise, commencing at the time determined by the Board.

10. Other Unit-Based Awards. The Board is authorized, subject to limitations under applicable law, to grant to Eligible Persons such other Awards that may be denominated or payable in, valued in whole or in part by reference to, or otherwise based on, or related to, Units, as deemed by the Board to be consistent with the purposes of this Plan, including, without limitation, unrestricted Units awarded purely as a "bonus" and not subject to any restrictions or conditions, other rights convertible or exchangeable into Units, purchase rights for Units, Awards with value and payment contingent upon performance of the Company or any other factors designated by the Board, and Awards valued by reference to the performance of specified Subsidiaries. The Board shall determine the terms and conditions of such Awards at date of grant or thereafter (subject to Section 15(d)). Units delivered pursuant to an Award in the nature of a purchase right granted under this Section 10 shall be purchased for such consideration, paid for at such times, by such methods, and in such forms, including, without limitation, cash, Units, notes or other property, as the Board shall determine. Cash awards, as an element of or supplement to any other Award under this Plan, shall also be authorized pursuant to this Section 10.

11. Substitute Awards. Awards granted under the Plan may, in the discretion of the Board, be granted to Eligible Persons in exchange or substitution for any other Award granted under the Plan or any award granted under any other plan or agreement of the Company or any Participating Affiliate, or any business entity to be acquired by the Company or any Participating Affiliate, or any other right of an Eligible Person to receive payment from the Company or any Participating Affiliate. The exercise price of any Award which is granted in connection with the substitution of awards granted under any other plan or agreement of the Company or any Participating Affiliate or any business entity to be acquired by the Company or any Participating Affiliate, shall be determined by the Board, in its discretion in a manner consistent with Section 409A of the Code.

12. Nontransferability of Awards. Unless otherwise expressly permitted by the Board in an Award Agreement or otherwise in writing, Awards may be assigned or otherwise transferred only in the following circumstances: (i) by will or the laws of descent and distribution; and (ii) by valid Beneficiary designation taking effect at death made in accordance with procedures established by the Board. Any Award held by a transferee will continue to be subject to the same terms and conditions that were applicable to the Award immediately prior to the transfer, except that the Award will be transferable by the transferee only by will or the laws of descent and distribution. A Participant's rights under the Plan may not be pledged, mortgaged, hypothecated, or otherwise encumbered, and shall not be subject to claims of the Eligible Person's creditors.

13. Call Right. Prior to a Qualified Public Offering, unless otherwise provided in an Award Agreement, the Company shall have the right to purchase from a Participant all vested Awards and Units held by the Participant upon the Participant's Termination of Service hereunder for any reason (a "Call Right"). The purchase price for Units will be the Fair Market Value of the underlying Units on the date of exercise of the Call Right (and the purchase price for Options and UARs will be the purchase price of the Units, less the Option exercise price). Unless otherwise provided in an Award Agreement, the Company's right to purchase the Awards and Units must be exercised by giving written notice of exercise to the Participant within eighteen (18) months following the Termination of Service of the Participant. The Company shall make payment for the unexercised Awards or Units in cash twenty (20) days after delivery of written notice of exercise of the purchase right and the determination of Fair Market Value.

14. Restrictive Covenants. The Board may, by way of the Award Agreements or otherwise, establish such other terms, conditions, restrictions and/or limitations, if any, of any Award, provided they are not inconsistent with this Plan, including, without limitation, the requirement that the Participant not engage in competition with, solicit customers or employees of, disclose or use confidential information of, or disparage the Company or its affiliates.

15. General Provisions.

(a) Compliance with Legal and Trading Requirements. The Plan, the granting and exercising of Awards thereunder, and the other obligations of the Company under the Plan and any Award Agreement, shall be subject to all applicable federal, state and foreign laws, rules and regulations, and to such approvals by any regulatory or governmental agency as may be required. The Company, in its discretion, may postpone the issuance or delivery of Units under any Award until completion of such stock exchange or market system listing or registration or qualification of such Units or other action under any state, federal or foreign law, rule or regulation as the Company may consider appropriate, and may require any Participant to make such representations and furnish such information as it may consider appropriate in connection with the issuance or delivery of Units in compliance with applicable laws, rules and regulations. No provisions of the Plan shall be interpreted or construed to obligate the Company to register any Units under federal, state or foreign law.

(b) No Right to Continued Employment or Service. Neither the Plan nor any action taken thereunder shall be construed as giving any employee, consultant, advisor or Board member the right to be retained in the employ or other service of the Company or any Participating Affiliate, nor shall it interfere in any way with the right of the Company or any Participating Affiliate to terminate any Participant's service at any time.

(c) Taxes. The Company or any Participating Affiliate is authorized to withhold from any Award granted, any payment relating to an Award under the Plan, including from a distribution of Units, or any payroll or other payment to an Eligible Person, amounts of withholding and other taxes due in connection with any transaction involving an Award, and to take such other action as the Board may deem advisable to enable the Company and Eligible Persons to satisfy obligations for the payment of withholding taxes and other tax obligations relating to any Award. This authority shall include authority to withhold or receive Units or other property and to make cash payments in respect thereof in satisfaction of an Eligible Person's tax obligations; provided, however, that the amount of tax withholding to be satisfied by withholding Units shall be limited to the minimum amount of taxes, including employment taxes, required to be withheld under applicable Federal, state, foreign and local law.

(d) Changes to the Plan and Awards. The Board may amend, alter, suspend, discontinue, or terminate the Plan or the Board's authority to grant Awards under the Plan without the consent of equity holders of the Company or Participants; provided, however, that, without the consent of an affected Participant, no amendment, alteration, suspension, discontinuation, or termination of the Plan may materially and adversely affect the rights of such Participant under any Award theretofore granted to the Participant. The Board may waive any conditions or rights under, amend any terms of, or amend, alter, suspend, discontinue or terminate, any Award theretofore granted, prospectively or retrospectively; provided, however, that, without the consent of a Participant, no amendment, alteration, suspension, discontinuation or termination of any

Award may materially and adversely affect the rights of such Participant under any Award theretofore granted to him or her.

(e) No Rights to Awards; No Member Rights. No Eligible Person or employee shall have any claim to be granted any Award under the Plan, and there is no obligation for uniformity of treatment of Eligible Persons. No Award shall confer on any Eligible Person any of the rights of a Unit holder of the Company unless and until Units are duly issued or transferred to the Eligible Person in accordance with the terms of the Award. In addition, no Unit shall confer on any Unit holder any of the rights of a Member of the Company unless and until such Unit holder is admitted to the Company as a Member of the Company.

(f) Nonexclusivity of the Plan. The adoption of the Plan by the Board shall not be construed as creating any limitations on the power of the Board to adopt such other incentive arrangements as it may deem desirable, including, without limitation, the granting of awards and other Awards otherwise than under the Plan, and such arrangements may be either applicable generally or only in specific cases.

(g) Not Compensation for Benefit Plans. No Award payable under this Plan shall be deemed salary or compensation for the purpose of computing benefits under any benefit plan or other arrangement of the Company for the benefit of Eligible Persons unless the Board shall determine otherwise.

(h) Section 409A. Awards under this Plan are intended to comply with, or be exempt from, the applicable requirements of Section 409A of the Code and shall be limited, construed and interpreted in accordance with such intent. Although the Company does not guarantee any particular tax treatment, to the extent that any Award is subject to Section 409A of the Code, it shall be paid in a manner that is intended to comply with Section 409A of the Code, including regulations and any other guidance issued by the Secretary of the Treasury and the Internal Revenue Service with respect thereto. In no event whatsoever shall the Company be liable for any additional tax, interest or penalties that may be imposed on a Participant by Section 409A of the Code or any damages for failing to comply with Section 409A of the Code.

(i) LLC Agreement. If Units are issued to a Participant when the Company is not a publicly-traded entity, simultaneous with the issuance of the Units, the Participant shall, as a condition to the Participant's right to receive the Units, become a party to the LLC Agreement by execution of a joinder agreement in form and substance satisfactory to the Company.

(j) Governing Law. The validity, construction, and effect of the Plan, any rules and regulations relating to the Plan, and any Award Agreement shall be determined in accordance with the laws of Delaware without giving effect to principles of conflict of laws.

(k) Effective Date; Plan Termination. The Plan shall become effective as of March 1, 2012 (the "Effective Date"). The Plan shall terminate as to future Awards on the date which is ten (10) years after the Effective Date.

(l) Titles and Headings. The titles and headings of the sections in the Plan are for convenience of reference only. In the event of any conflict, the text of the Plan, rather than such titles or headings, shall control.

DOC 3 Header

**Second Amendment to
Amended and Restated Limited Liability Agreement of
Colt Defense LLC**

This SECOND AMENDMENT (this "Amendment"), dated as of March 1, 2012, to the Amended and Restated Limited Liability Agreement, dated as of June 12, 2002, as amended July 9, 2007 (as so amended, the "LLC Agreement"), for Colt Defense LLC (the "Company") is entered into by the Governing Board (the "Board") of the Company on behalf of the Company and the Members identified on the signature pages hereto, representing Common Members holding greater than 50% of the voting Equity Securities held by such Common Members in accordance with Section 14.2 of the LLC Agreement.

RECITALS

WHEREAS, the Company desires to enter into a long term incentive plan ("LTIP") which provides for the issuance of a new series of Common Units on the terms described herein (the "Class B Common Units") and amend the LLC Agreement, to provide for the issuance of the Class B Common Units in accordance with the LTIP;

WHEREAS, pursuant to Sections 14.2 and 5.9.7 of the Company's LLC Agreement, the Company is required to obtain the consent of Colt Defense Holding LLC ("C-Defense Holding"), Blackstone Mezzanine Partners II-A L.P. ("BMP") and Blackstone Mezzanine Holdings II USS L.P. (collectively, "Blackstone") in certain circumstances;

WHEREAS, the Company has obtained approval and consent for this Amendment from C-Defense Holding and Blackstone, as evidenced by their signature page to this Amendment attached hereto;

WHEREAS, the Board has determined that the issuance of the Class B Common Units provided for in this Amendment is in the best interests of the Company;

NOW, THEREFORE, in consideration of the foregoing, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto hereby agree as follows:

Section 1. Definitions. Capitalized terms used but not otherwise defined herein shall have the meanings assigned thereto in the LLC Agreement.

Section 2. Amendment. The LLC Agreement is hereby amended as follows:

a. Article I of the LLC Agreement is hereby amended by

(i) amending and restating the following definitions:

"Common Member" means a Member that holds one or more Common Units or Class B Common Units.

“Permitted Issuance” means (i) the issuance of Equity Equivalents as a unit dividend or other distribution or upon any subdivision, split or combination of all of the outstanding Units; (ii) the issuance of Equity Equivalents upon conversion, exchange or redemption of any convertible or exchangeable securities outstanding on the date hereof or which were issued in compliance with Section 4.5; (iii) the issuance of Equity Equivalents to acquire Common Units or Class B Common Units to any employee, consultant or board member of the Company or any of its subsidiaries (in each case, other than Sciens or Blackstone or their respective Affiliates or employees) pursuant to any equity incentive plan approved and adopted by the Governing Board (provided, that the aggregate of all such issuances as of the time of determination (including the proposed issuance) shall not exceed 18,878 Units (as equitably adjusted for any distributions of Units, in each case, on the Common Units or Class B Common Units or subdivision or reclassification of such Common Units or Class B Common Units), *provided* that the allocation of such Units between Common Units and Class B Common Units shall be expressly authorized and determined by resolution of the Governing Board; (iv) the issuance to any Person that is not a Member of an Affiliate of a Member of Equity Equivalents as consideration (whether partial or otherwise) for the purchase by the Company or any of its subsidiaries of assets, stock or other equity securities of any Person, whether in a merger, acquisition, joint venture or otherwise; (v) the issuance of Equity Equivalents by any of the Company’s wholly-owned subsidiaries to the Company or any other wholly-owned subsidiary of the Company; and (vi) the issuance of any Equity Equivalents to financial institutions, banks or equipment lessors (in each case, other than Sciens or Blackstone or their respective Affiliates), in connection with bona fide loans from them to the Company or its subsidiaries.

(ii) inserting the following new definitions in appropriate alphabetical order:

“Class B Common Units” means up to 18,878 Units of the Company having identical terms to the Common Units authorized and issued as of the date of this Amendment; provided, that under no circumstance shall the Class B Common Units have the rights attributed to Common Units under Section 4.2.2 or any other voting rights hereunder.”

“LTIP” means the Long Term Incentive Plan entered into by the Company on March 1, 2012.

b. Article IV of the LLC Agreement is hereby amended as follows:

i. The last sentence in Section 4.1 is hereby replaced by the following:

“The total number of Units of all series that the Company has authority to issue is 1,250,000 consisting of 1,000,000 Common Units (“**Common Units**”), as further described below in Section 4.2, which shall include 18,878 nonvoting Common Units (“**Class B Common Units**”) as further described below in Section 4.1.3 and 250,000 Preferred Units (the “**Preferred**

Units”), 250,000 of which are on the date of this amendment undesignated.”

- ii. The addition of new Section 4.1.3, describing the new series of Class B Common Units:

“4.1.3 Class B Common Units Generally. Class B Common Units will be a new series of Common Units under this Agreement, having all the rights and attributes of Common Units, except for voting rights under section 4.2.2. In connection with any transfer, assignment or sale to a bona fide third party purchaser after the consummation of a Qualified Public Offering approved in accordance with this Agreement, the outstanding Class B Common Units will be converted or exchanged into Equity Securities of the same class or series as the securities being offered in such Qualified Public Offering (“*IPO Securities*”), such that holders of the Class B Common Units will receive IPO Securities having a value equal to the same proportion of the aggregate pre-Qualified Public Offering value, if any, that such holder would have received if all of the Company’s cash and other property had been distributed by the Company in complete liquidation pursuant to the rights and preferences set forth in Section 8.1 as in effect immediately prior to such distribution. Notwithstanding anything in this Agreement to the contrary, the holders of the Class B Common Units will not be considered “Members” for the purposes of Sections 3.2, 3.3.4, 3.3.5, 3.3.6, 3.3.7, 4.3.5, 4.5, 5.4, 5.5, 5.6, 5.8, 6.1.2, 6.1.3 and 12.4 and will not be entitled to exercise the rights of Members set forth in such Sections.

- iii. Section 4.3.6 is hereby amended by adding “(if they are entitled to vote)” after “Units” the third time it appears in such Section.
- iv. Section 7.4 is hereby amended and restated by adding “and Class B Common Units” after “Common Units” in the first sentence.
- v. Section 7.5.2 is hereby amended and restated by adding “and Class B Common Units” after “Common Units” each time it appears in such Section.
- vi. Section 8.2 is hereby amended and restated by adding “and Class B Common Units” after “Common Units” each time it appears in the first and second sentences and by adding “and Class B Common Unit” after “Common Unit” in the second sentence.

Section 3. Continuation. This Amendment shall be deemed to be part of, and a modification to, the LLC Agreement and shall be governed by the terms of the LLC Agreement, which terms are incorporated herein by reference, are ratified and confirmed and shall continue

in full force and effect. Except as set forth herein, the LLC Agreement shall remain in full force and effect and not otherwise be modified or affected by the provisions hereof.

Section 4. Counterparts. This Amendment may be executed in multiple counterparts, each of which shall be deemed an original, but all of which, taken together, shall constitute one and the same instrument.

Section 5. Governing Law. This Amendment shall be enforced, governed and construed in all respects in accordance with the internal laws of the State of Delaware, without giving effect to the choice of law or conflict of law rules or laws of such jurisdiction.

[Signature Page Follows]

IN WITNESS WHEREOF, the parties hereto, intending to be legally bound hereby, have caused this Amendment to be executed in counterparts as of the day and year first written above.

COLT DEFENSE HOLDING LLC

By: Sciens Management LLC, its Manager

By: /s/ John P. Rigas

Name: John P. Rigas

Title: Authorized Signatory

CDH II LLC

By: Colt Defense Holding LLC, a manager

By: Sciens Management LLC, the manager of Colt Defense Holding LLC

By: /s/ John P. Rigas

Name: John P. Rigas

BLACKSTONE MEZZANINE PARTNERS II - A L.P.
BY: BLACKSTONE MEZZANINE ASSOCIATES II LP, ITS
GENERALPARTNER
BY: BLACKSTONE MEZANINE MANAGEMENT
ASSOCIATES II USS LLC
ITS: GENERAL PARTNER
By: /s/ Maria J. Beeney
Name: Maria J. Beeney
Title: Authorized Signatory

BLACKSTONE MEZZANINE HOLDINGS II USS L.P
BY: BMP II USS SIDE-BY-SIDE GP LLC
ITS: GENERAL PARTNER
By: /s/ Maria J. Beeney
Name: Maria J. Beeney
Title: Authorized Signatory

COLT DEFENSE LLC,
a Delaware Limited Liability Company

By: /s/ Jeffrey G. Grody
Name: Jeffrey G. Grody
Title: General Counsel and Secretary

DOC 4 Header

**Certification of Chief Executive Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Gerald R. Dinkel, certify that:

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

Date: May 2, 2012

/s/ Gerald R. Dinkel

Gerald R. Dinkel

President and Chief Executive Officer

DOC 5 Header

**Certification of Chief Financial Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Scott B. Flaherty, certify that:

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

Date: May 2, 2012

/s/ Scott B. Flaherty

Scott B. Flaherty

Senior Vice President and Chief Financial Officer

DOC 6 Header

**Certification of Chief Accounting Officer
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Cynthia J. McNickle, certify that:

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

Date: May 2, 2012

/s/ Cynthia J. McNickle

Cynthia J. McNickle

Vice President and Chief Accounting Officer

DOC 7 Header

coltdef-20120401.xml

DOC 8 Header

coltdef-20120401.xsd

DOC 9 Header

coltdef-20120401_cal.xml

DOC 10 Header

coltdef-20120401_def.xml

DOC 11 Header

coltdef-20120401_lab.xml

DOC 12 Header

coltdef-20120401_pre.xml