

Megadiamond Industries, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - CONTINUED

April 30, 1980

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Organization Expense

Organization expense is being amortized over a five-year period.

NOTE B - PRIOR PERIOD ADJUSTMENT - RESTATEMENT OF INVENTORY

During the year, the parent company restated its beginning inventory to properly reflect its inventory at the lower of cost or market, by a write down of slow moving sintered diamond inventory. This resulted in a restatement in beginning retained earnings of \$257,852.

NOTE C - ACCOUNTING CHANGES - LEASES

During the year, the company changed its method of accounting for leased property under capitalized leases to be in conformity with Financial Accounting Standards Board statements #13 and #17, which established new standards of accounting for capital leases. The company's retained earnings, as of May 1, 1979, has been restated by \$3,987 to give retroactive effect for the change in accounting as if statements #13 and #17 had been in effect for prior years. The change in accounting involved the capitalization of equipment obligations at discounted amounts totaling \$289,450; the amortization of the related lease assets over the lease periods which approximate the lives of the equipment; the reduction of the lease obligations by monthly lease payments, net of charges to interest expense; and the recognition of the deferred income tax effects.

The effect of the change on earnings for the year ended April 30, 1980 is immaterial.

NOTE D - NOTES PAYABLE - BANKS

Notes payable - banks, at April 30, 1980, are comprised of the following:

Line of credit agreement	\$ 988,818
Demand note payable	250,000
	<u>\$1,238,818</u>

In 1979, the line of credit agreement was entered into with a bank. The agreement provides for borrowings up to \$2,000,000 with certain restrictions, at an interest rate of the greater of 3-1/3% over the bank's prime interest rate or 1/2% over the latest three-week moving average commercial paper rate. Interest is paid monthly.