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SCIENCE - ENGINEERING - TECHNOLOGY — CONSULTING - DESIGN - CONSTRUCTION

H. TRACY HALL, INCORPORATED

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SUBJECT: PROPOSED LEASE AGREEMENT WITH DBT INC.

Cost estimates:	New steel material	$25,000
	Machine time	$50,000
	Design	$10,000
	Misc. Parts	$ 5,000
	Overhead attributed to press manufacture	$15,000
	Assembly and delivery	$10,000
Total estimated cost		$115,000

Basis for royalties =250,000 dollars. This will create a additional 25,000 dollar cost.

TOTAL COST INCLUDING ROYALTY PAYMENT:
$140,000

New capital which must be raised in order to build press = $140,000.

This capital investment will yield us an investment credit of $14,000 the first year which can be deducted from taxes owed if we have sufficient profit. In order to have sufficient profit the first year (Aug. 1977-Aug. 1978) We would need to sell another press during that time and achieve an income level above 100,000 dollars.

Using st. line depreciation, we will be able to deduct 20,000 dollars each year from our lease revenue. The payment on the $140,000 dollar loan at 10% would be $2,304.96/month or $27,659.04/year. Interest on the loan is deductable and will decrease each year. The following table is based on a lease agreement of $4,500/month for seven years which is equivalent to $273,323.88 present value paid off monthly for seven years at 10%.

Income	Lease payments	Interest	depreciation	total payment owed on 140,000 debt.	Year
$20,643.78	$54,000	$13,356.22	$20,000	$27,659.52	1977
$22,141.52	54,000	11,858.48	"	"	1978
$23,796.10	"	10,203.90	"	"	1979
$25,623.93	"	8,376. 07	"	"	1980
$27,643.16	"	6,356. 84	"	"	1981
$29,873.83	"	4,126. 17	"	"	1982
$32,338.08	"	1,661. 92	"	"	1983

Cash flow into the company each year is constant at$26,340.48

By building and leasing a 1000 ton press to DBT at 4500.00 per month for seven years we will be able to cover operating expenses of our shop with one machinist and one part time helper plus overhead for seven years without producing a profit from the operation of the company during that period. This effort would ensure continuous operation of the company shop for seven years giving us pleanty of time to develop other profitable products. It is probable that Mega and DBT will need additional equipment in future years which we could build and lease to them on a similar basis. A second press could provide a long term income to provide wages for yourself or additional employees or equipment.

In order to lease equipment to DBT H.T.H. inc. would have to be a normal corporation. A sub chapter S company cannot have rental income to this extent. As I have discussed with you previously, a normal corporation is superior to sub.S if you want to purchase additional equipment or retain earnings for other projects.

The steps which need to be completed before submitting a formal proposal to DBT are the following.

1. Check availability of JIM H. shop for estimate of delivery.
2. Perform initial design concept so that press can be described.
3. Check with IRS on acceptability of lease, change to normal corporation, depreciation schedule, capital investiment transfer to lessee, and capital investment basis. Check also with accountant and lawyer.
4. Check with research corporation about payment of royalties. (basis?)
5. obtain source for $140,000 needed for manufacture of press.
6. Find out if a good machinist is available for hire for our shop and also if there will be good talent avaialble at JIM H. shop.
7. have lawyer draw up lease agreement.
8. submit preliminary proposal to DBT (before step 7)
9. Obtain requirements from DBT press operators etc. for specific design requirements and suggestions. (after submitting first proposal with our design ideas)

Step 7 is the final step and is the formal proposal.

David Hall