Suprajit USA, Inc.

Independent Auditor’s Report and Consolidated Financial Statements

March 31, 2020 and 2019

Suprajit USA, Inc.
March 31, 2020 and 2019

Contents

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Independent Auditor's Report

Board of Directors
Suprajit USA, Inc.

We have audited the accompanying consolidated financial statements of Suprajit USA, Inc. (a 100% wholly-owned subsidiary of Suprajit Engineering Limited) and its subsidiary, which comprise the consolidated balance sheets as of March 31, 2020 and 2019, and the related consolidated statements of operations and comprehensive loss, stockholder's equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Suprajit USA, Inc. and its subsidiary as of March 31, 2020 and 2019, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

As discussed in *Note 7* to the financial statements, in 2020, the entity adopted new accounting guidance for accounting for leases. Our opinion is not modified with respect to this matter.

As discussed in *Note 8* to the financial statements, in 2020, the entity adopted new accounting guidance regarding recognition of revenue with customers. Our opinion is not modified with respect to this matter.

Other Matter – Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The consolidating schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

BKD, LLP

Wichita, Kansas
June 5, 2020

Suprajit USA, Inc.
Consolidated Balance Sheets
March 31, 2020 and 2019

Assets

	2020	2019
Current Assets		
Cash	$ 1,813,130	$ 1,380,299
Accounts receivable, net of allowance; 2020 - $22,188, 2019 - $32,942	3,265,172	3,987,548
Inventories	7,119,152	10,533,276
Prepaid expenses and other	305,027	370,536
Refundable income taxes	314,163	225,546
Total current assets	12,816,644	16,497,205
Property and Equipment, at Cost		
Land and land improvements	579,766	579,766
Buildings and leasehold improvements	2,932,930	2,601,102
Machinery and equipment	6,248,418	6,150,497
Office equipment	1,232,721	1,177,429
Transportation equipment	44,097	44,097
Construction in progress	8,838	65,415
	11,046,770	10,618,306
Less accumulated depreciation and amortization	(4,269,544)	(3,015,315)
	6,777,226	7,602,991
Other Assets		
Goodwill	10,900,978	12,594,699
Indefinite-lived intangible assets	1,420,000	1,420,000
Definite-lived intangible assets	12,114,515	13,398,361
	24,435,493	27,413,060
Total assets	$ 44,029,363	$ 51,513,256

See Notes to Consolidated Financial Statements

Liabilities and Stockholder's Equity

	2020	2019
Current Liabilities		
Current maturities of long-term debt	$ 6,250,000	$ 6,250,000
Line of credit	7,000,000	4,820,000
Accounts payable	3,481,202	4,984,575
Accrued interest	42,025	87,936
Accrued salaries, wages and commissions	354,643	291,450
Accrued vacation	393,552	437,018
Operating lease liability	262,338	-
Accrued other	216,892	208,758
Total current liabilities	18,000,652	17,079,737
Long-term Liabilities		
Long-term debt, less current maturities	2,459,408	7,432,347
Interest rate swap agreement	113,850	4,429
Deferred income taxes	3,920,622	4,613,400
Other long-term liabilities	221,222	321,931
Total long-term liabilities	6,715,102	12,372,107
Stockholder's Equity		
Preferred stock, $10.00 par value; authorized 1,000,000 shares, issued - none	-	-
Common stock, $1.00 par value; 10,000 shares authorized, 1,000 shares issued and outstanding	1,000	1,000
Additional paid-in capital	20,999,000	20,999,000
Retained earnings	(1,596,449)	1,064,911
Accumulated other comprehensive loss	(89,942)	(3,499)
Total stockholder's equity	19,313,609	22,061,412
Total liabilities and stockholder's equity	$ 44,029,363	$ 51,513,256

Suprajit USA, Inc.

Consolidated Statements of Operations and Comprehensive Loss

Years Ended March 31, 2020 and 2019

	2020	2019
Net Sales	$ 37,432,345	$ 40,960,674
Cost of Goods Sold	32,788,944	33,275,713
Gross Profit	4,643,401	7,684,961
Selling, General and Administrative Expenses	7,241,583	8,266,107
Operating Loss	(2,598,182)	(581,146)
Other Expense		
Interest expense	(795,595)	(970,664)
Other	(35,891)	(20,647)
	(831,486)	(991,311)
Loss Before Income Taxes	(3,429,668)	(1,572,457)
Benefit for Income Taxes	(768,308)	(384,099)
Net Loss	(2,661,360)	(1,188,358)
Other Comprehensive Loss		
Change in fair value of rate swap agreement, net of taxes of $(22,978) in 2020 and $(9,287) in 2019	(86,443)	(34,936)
Comprehensive Loss	$ (2,747,803)	$ (1,223,294)

Suprajit USA, Inc.

Consolidated Statements of Stockholder's Equity

Years Ended March 31, 2020 and 2019

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, April 1, 2018	$ 1,000	$ 20,999,000	$ 2,253,269	$ 31,437	$ 23,284,706
Net loss	-	-	(1,188,358)	-	(1,188,358)
Other comprehensive loss, net	-	-	-	(34,936)	(34,936)
Balance, March 31, 2019	1,000	20,999,000	1,064,911	(3,499)	22,061,412
Net loss	-	-	(2,661,360)	-	(2,661,360)
Other comprehensive loss, net	-	-	-	(86,443)	(86,443)
Balance, March 31, 2020	$ 1,000	$ 20,999,000	$ (1,596,449)	$ (89,942)	$ 19,313,609

Suprajit USA, Inc.
Consolidated Statements of Cash Flows
Years Ended March 31, 2020 and 2019

	2020	2019
Operating Activities		
Net loss	$ (2,661,360)	$ (1,188,358)
Items not requiring (providing) cash		
Depreciation and amortization	4,607,452	4,269,041
Amortization of debt issuance costs	27,061	27,061
Loss on sale of property and equipment	25,342	30,267
Deferred income taxes	(669,800)	(409,870)
Changes in		
Accounts receivable	722,376	3,098,316
Inventories	3,414,124	(1,975,264)
Related party receivables/payables	(6,075)	(39,221)
Prepaid expenses and other	65,509	50,759
Income tax refundable	(88,617)	(685,429)
Accounts payable	(1,503,373)	1,442,325
Operating lease liability	(349,784)	-
Accrued liabilities	(112,684)	(767,014)
Net cash provided by operating activities	3,470,171	3,852,613
Investing Activities		
Purchase of property and equipment	(217,340)	(1,266,835)
Net cash used in investing activities	(217,340)	(1,266,835)
Financing Activities		
Borrowings under line-of-credit agreement	9,479,000	19,040,000
Payments under line-of-credit agreement	(7,299,000)	(16,630,000)
Principal payments on long-term debt	(5,000,000)	(5,000,000)
Net cash used in financing activities	(2,820,000)	(2,590,000)
Increase (Decrease) in Cash	432,831	(4,222)
Cash, Beginning of Year	1,380,299	1,384,521
Cash, End of Year	$ 1,813,130	$ 1,380,299
Supplemental Cash Flows Information		
Interest paid	$ 814,445	$ 970,306
Income taxes paid (refunded)	$ (9,891)	$ 711,225
ROU assets obtained in exchange for new operating lease liabilities	$ 612,122	$ -

Suprajit USA, Inc.
Notes to Consolidated Financial Statements
March 31, 2020 and 2019

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Suprajit USA, Inc. (“Company”), through its wholly-owned subsidiary, earns revenues predominately from the manufacturing of high performance mechanical controls for the outdoor power equipment, recreational vehicle, agricultural and construction equipment markets. Products are sold primarily to manufacturers in the United States.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Wescon Controls LLC (“Wescon”). All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

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

Cash

The Company maintains cash balances at financial institutions which from time to time may exceed federally insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash.

Accounts Receivable

Accounts receivable are stated at the amount of consideration due from customers, the majority of which are original equipment manufacturers, of which the Company has an unconditional right to receive plus any accrued and unpaid interest. Credit is extended based on an evaluation of a customer’s financial condition; generally, collateral is not required. The Company provides an allowance for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information, the customer’s current ability to pay its obligations to the Company and existing economic conditions.

Accounts receivable are ordinarily due 30 days after the issuance of the invoice for the majority of customers and up to 120 days for certain customers. Accounts outstanding longer than the agreed payment terms are considered delinquent. Delinquent receivables are written off based on individual credit evaluation and specific circumstances of the customer.

Inventories

Inventories consist of raw materials, work in process and finished goods. Inventories are stated at the lower of standard cost or net realizable value using the FIFO (first-in, first-out) method.

Property and Equipment

Property and equipment acquisitions are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is charged to expense on the straight-line basis over the estimated useful life of each asset. Leasehold improvements and ROU assets under operating leases are amortized over the shorter of the lease term or their respective estimated useful lives.

The estimated useful lives for each major depreciable classification of property and equipment are as follows:

Land improvements	20 years
Buildings and leasehold improvements	10 - 20 years
Machinery and equipment	2 - 10 years
Office equipment	3 - 10 years
Transportation equipment	3 - 5 years

Depreciation and amortization expense totaled $1,629,885 and $1,291,474 for the years ended March 31, 2020 and 2019, respectively.

Goodwill

The Company has elected the private company accounting alternative for the subsequent measurement of goodwill. Under this alternative, goodwill is amortized on a straight-line basis over 10 years. The Company evaluates the recoverability of the carrying value of goodwill at the entity level whenever events or circumstances indicate the carrying amount may not be recoverable.

In testing goodwill for impairment, the Company has the option first to perform a qualitative assessment to determine whether it is more likely than not that goodwill is impaired or the entity can bypass the qualitative assessment and proceed directly to the quantitative test by comparing the carrying amount, including goodwill, of the entity with its fair value. The goodwill impairment loss, if any, is measured as the amount by which the carrying amount of an entity, including goodwill, exceeds its fair value. Subsequent increases in goodwill value are not recognized in the financial statements.

Intangible Assets

Intangible assets with finite lives are being amortized on the straight-line basis over periods ranging from 1 to 13 years. Such assets are periodically evaluated as to the recoverability of their carrying values.

Indefinite-lived intangibles include trade names. Trade names are not subject to amortization, but are tested for impairment on an annual basis or whenever an impairment indicator is identified. The Company performs its annual impairment testing in the fourth quarter for all indefinite-lived intangibles.

Interest Rate Swaps

The Company has elected the private company accounting alternative for certain interest rate swaps. The election to use the alternative accounting for interest rate swaps is made on a swap-by-swap basis. During 2020 and 2019, the Company had one interest rate swap in effect for which it elected to apply the alternative accounting and use the simplified hedge accounting approach.

Long-lived Asset Impairment

The Company evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

No asset impairment was recognized during 2020 or 2019.

Deferred Financing Costs

Deferred financing costs comprise the direct costs associated with obtaining financing and are amortized over the life of the debt using a method that approximates the effective interest method. Amortization expense of deferred financing costs was $27,061 for both years ending March 31, 2020 and 2019, and is included in interest expense. Total accumulated amortization at March 31, 2020 and 2019, was $94,714 and $67,653, respectively.

The net deferred financing cost of $40,592 related to long-term debt is offsetting debt in the long-term liabilities section on the consolidated balance sheet.

Income Taxes

The Company accounts for income taxes in accordance with income tax accounting guidance (Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 740, *Income Taxes*). The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Company determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is

based on the tax effects of the differences between the book and tax bases of assets and liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur. Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

Tax positions are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. The term more likely than not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any. A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances and information available at the reporting date and is subject to the management's judgment.

The Company recognizes interest and penalties on income taxes as a component of income tax expense. The Company files consolidated income tax returns with its subsidiary.

Revenue Recognition

Revenue is recognized when control of the promised goods or services is transferred to the Company's customers, in an amount that reflects the consideration that it expects to be entitled to in exchange for those goods or services. The amount and timing of revenue recognition varies based on the nature of the goods or services provided and the terms and conditions of the customer contract. See *Note 8* for additional information about the Company's revenue.

Shipping and Handling Costs

Shipping and handling fees charged to customers are included in net sales. Shipping and handling costs are included in cost of goods sold.

Comprehensive Income (Loss)

Comprehensive income consists of net income (loss) and other comprehensive income (loss), net of applicable income taxes. Other comprehensive income (loss) includes unrealized and realized gains and losses for the interest rate swap that qualifies for hedge accounting.

Subsequent Events

As a result of the spread of the SARS-CoV-2 virus and the incidence of COVID-19, economic uncertainties have arisen which may negatively affect the financial position, results of operations and cash flows of the Company. The duration of these uncertainties and the ultimate financial effects cannot be reasonably estimated at this time.

On March 27, 2020, President Trump signed into law the *Coronavirus Aid, Relief, and Economic Security Act*. On May 4, 2020, the Company received a loan in the amount of approximately $2.2 million pursuant to the Paycheck Protection Program.

Subsequent events have been evaluated through June 5, 2020, which is the date the financial statements were available to be issued.

Note 2: Inventories

Inventory consisted of the following at March 31, 2020 and 2019:

	2020	2019
Manufacturing inventories		
Raw materials	$ 5,881,010	$ 7,222,571
Work-in-process and finished goods	2,151,914	4,005,426
	8,032,924	11,227,997
Reserve for obsolescence	(913,772)	(694,721)
	$ 7,119,152	$ 10,533,276

During 2019, the Company changed its estimate on its reserve for obsolescence. As part of this change, the Company increased from 50% to 100% its reserve over certain inventory items that are slow moving or reflected no activity in the most recent year. The impact of this change increased its reserve by $347,361 in 2019. During 2020 the Company further enhanced its reserve policy for slow moving inventory items which increased the reserve by approximately $520,000.

Note 3: Acquired Intangible Assets and Goodwill

The carrying basis and accumulated amortization of recognized intangible assets at March 31, 2020 and 2019, were:

		2020		2019	
	Weighted Average Amortization Period	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Definite-lived intangible assets					
Customer relationships	13 years	$ 16,690,000	$ 4,575,485	$ 16,690,000	$ 3,291,639
Non-compete agreements	1 year	160,000	160,000	160,000	160,000
Goodwill	10 years	16,937,212	6,036,234	16,937,212	4,342,513
		$ 33,787,212	$ 10,771,719	$ 33,787,212	$ 7,794,152
Indefinite-lived intangible assets					
Tradename		$ 1,420,000		$ 1,420,000	

Amortization expense for the years ended March 31, 2020 and 2019, was $2,977,567 for both years. Estimated amortization expense for each of the following five years is:

2021	$ 2,977,567
2022	2,977,567
2023	2,977,567
2024	2,977,567
2025	2,977,567

Note 4: Line of Credit

The Company has a $8,750,000 revolving line of credit expiring in August 2020. At March 31, 2020 and 2019, there was $7,000,000 and $4,820,000 borrowed against this line, respectively. The line is collateralized by substantially all of the Company's assets and is guaranteed by the Parent, Suprajit Engineering Limited. Interest varies with the LIBOR rate plus 2.75%, which was 3.75% and 5.25% on March 31, 2020 and 2019, respectively.

In connection with this line of credit and term loan (see *Note 5*), the Company's Parent, Suprajit Engineering Limited, is required, among other things, to maintain certain financial conditions, including maintaining a consolidated debt service coverage, and a consolidated leverage ratio.

While the line of credit has a due date within one year of the issuance of these financial statements, the Company utilizes the financing for long-term operating purposes and does not have liquid funds available to repay the balance at maturity. Management intends to renew the line of credit on comparable terms at or near the maturity date and believes it is probable such renewal will be successful.

Note 5: Long-term Debt

The Company has a term loan with a bank expiring in September 2021; principal payments are due in quarterly installments of $1,250,000, including interest at the LIBOR rate plus 2.30%. Unamortized debt issuance costs were $40,592 and $67,653 at March 31, 2020 and 2019, respectively. The effective interest rate was 3.75% and 4.82% for the years ended March 31, 2020 and 2019, respectively. At March 31, 2020 and 2019, the outstanding balance of the loan was $8,750,000 and $13,750,000, respectively. The line is collateralized by substantially all of the Company’s assets and is guaranteed by the Parent, Suprajit Engineering Limited.

Annual maturities of long-term debt payments at March 31, 2020, are:

2021	$ 6,250,000
2022	2,500,000
	$ 8,750,000

Note 6: Derivative Financial Instruments

Interest Rate Swap

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations, the Company entered into an interest rate swap agreement during 2018 for a portion of its floating rate debt. The agreement provides for the Company to receive interest from the counterparty at LIBOR and to pay interest to the counterparty at a fixed rate of 2.42% on amortizing notional amounts of $7,500,000 at March 31, 2020. Under the agreement, the Company pays or receives the net interest amount quarterly, with the quarterly settlements included in interest expense. The agreement ends on September 8, 2021.

Management has designated the interest rate swap agreement as a cash flow hedging instrument. For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings.

With the adoption of Accounting Standards Update 2014-03, Derivatives and Hedging (Topic 815): *Accounting for Certain Receive – Variable, Pay Fix Interest Rate Swaps – Simplified Hedge Accounting Approach*, the Company can assume no ineffectiveness for qualifying swaps when applying hedge accounting under Topic 815.

The table below presents certain information regarding the Company's interest rate swap agreement designated as a cash flow hedge. The Company did not have any derivative instruments at March 31, 2020 and 2019, which were not designated as hedging instruments.

		2020	**2019**
	Balance sheet location of fair value amount		
Fair value of interest rate swap	Other long-term liabilities	$ (113,850)	$ (4,429)
	Income statement location		
Loss reclassified from accumulated other comprehensive income into income (monthly settlement)	Interest expense	$ 15,768	$ 3,092

Note 7: Leases

Change in Accounting Principle

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. This ASU requires lessees to recognize a lease liability and a right-of-use (ROU) asset on a discounted basis, for substantially all leases, as well as additional disclosures regarding leasing arrangements. Disclosures are required to enable users of financial statements to assess the amount, timing and uncertainty of cash flows arising from leases. In July 2018, the FASB issued ASU 2018-11, *Leases (Topic 842): Targeted Improvements*, which provides an optional transition method of applying the new lease standard. Topic 842 can be applied using either a modified retrospective approach at the beginning of the earliest period presented or, as permitted by ASU 2018-11, at the beginning of the period in which it is adopted, *i.e*., the comparatives under ASC 840 option.

The Company adopted Topic 842 on April 1, 2019 (the effective date), using the comparatives under ASC 840 transition method, which applies Topic 842 at the beginning of the period in which it is adopted. Prior period amounts have not been adjusted in connection with the adoption of this standard. The Company elected the package of practical expedients under the new standard, which permits entities to not reassess lease classification, lease identification or initial direct costs for existing or expired leases prior to the effective date. Also, the Company elected to keep short-term leases with an initial term of 12 months or less off the balance sheet. The Company did elect the hindsight practical expedient in determining the lease term for existing leases as of April 1, 2019.

The most significant impact of adoption was the recognition of operating lease ROU assets and operating lease liabilities of $612,122 each. The standard did not significantly affect the consolidated statements of operations and comprehensive loss or cash flows.

The cumulative effect of the changes made to our consolidated balance sheets for the adoption of this standard was as follows:

	March 31, 2019 As Reported	ASC 842 Adjustment April 1, 2019	April 1, 2019 As Adjusted
Assets			
Right-of-use assets - operating leases	$ -	$ 612,122	$ 612,122
Liabilities			
Current portion of operating lease liabilities	-	(349,784)	(349,784)
Long-term portion of operating lease liabilities	-	(262,338)	(262,338)
Equity			
Retained earnings	1,064,911	-	1,064,911

Accounting Policies

The Company determines if an arrangement is a lease or contains a lease at inception. Leases result in the recognition of ROU assets and lease liabilities on the consolidated balance sheets. ROU assets represent the right to use an underlying asset for the lease term, and lease liabilities represent the obligation to make lease payments arising from the lease, measured on a discounted basis. The Company determines lease classification as operating or finance at the lease commencement date.

The Company combines lease and nonlease components, such as common area and other maintenance costs, in calculating the ROU assets and lease liabilities for its office buildings and employee vehicles.

At lease inception, the lease liability is measured at the present value of the lease payments over the lease term. The ROU asset equals the lease liability adjusted for any initial direct costs, prepaid or deferred rent, and lease incentives. As the leases did not provide an implicit rate, the Company used its incremental borrowing rate based on the information available at the commencement date to determine the present value of lease payments.

The lease term may include options to extend or to terminate the lease that the Company is reasonably certain to exercise. Lease expense is generally recognized on a straight-line basis over the lease term.

The Company has elected not to record leases with an initial term of 12 months or less on the consolidated balance sheets. Lease expense on such leases is recognized on a straight-line basis over the lease term.

Nature of Leases

The Company has entered into the following lease arrangements:

Operating Leases

The Company leases two facilities for manufacturing and warehouse space that expire in December 2020. There are no remaining lease renewal options under the agreement. Termination of the leases is generally prohibited unless there is a violation under the lease agreement.

All Leases

The Company has no material related-party leases.

The Company's lease agreements do not contain any material residual value guarantees or material restrictive covenants.

Quantitative Disclosures

The ROU assets obtained in exchange for new operating lease liabilities as of April 1, 2019, was $612,122 and is classified within Buildings and leasehold improvements in the consolidated balance sheets. The net ROU asset was $262,338 as of March 31, 2020. Operating lease cost for the year ended March 31, 2020, was $362,752. Future minimum lease payments at March 31, 2020, are $272,064 for 2021.

Note 8: Revenue from Contracts with Customers

Change in Accounting Principle

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, that replaces existing revenue recognition guidance. The new standard requires companies to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In addition, Topic 606 requires disclosures of the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

The Company adopted this standard on April 1, 2019, using a modified retrospective approach with the cumulative effect of initially applying the new standard recognized in retained earnings at the beginning of the year of adoption. Comparative prior period information has not been adjusted and continues to be reported in accordance with previous revenue recognition guidance in ASC Topic 605 – *Revenue Recognition.* The Company has applied the new standard to all contracts not complete at the date of adoption.

The Company's adoption of Topic 606 did not result in a change to the timing of revenue recognition.

Performance Obligations

Revenue is measured as the amount of consideration the Company expects to receive in exchange for transferring distinct goods or providing services to customers. The Company's revenue consists substantially of mechanical controls sales and is reported net of sales discounts, rebates, incentives, returns and other allowances offered to customers. The Company recognizes revenue when performance obligations under the terms of contracts with its customers are satisfied, which occurs when control passes to a customer to enable them to direct the use of and obtain benefit from a product. This typically occurs when a customer obtains legal title, obtains the risks and rewards of ownership, has received the goods according to the contractual shipping terms either at the shipping point or destination and is obligated to pay for the product. All of the Company's revenue is recognized at a point in time. Customary terms require payment within 30 days, and for certain customers, deposits may be required in advance of shipment.

Accounting Policies and Practical Expedients Elected

For shipping and handling activities, the Company is applying an accounting policy election, which allows an entity to account for shipping and handling activities as fulfillment activities rather than a promised good or service when the activities are performed, even if those activities are performed after the control of the good has been transferred to the customer. Therefore, the Company expenses shipping and handling costs at the time revenue is recognized. The Company classifies shipping and handling expenses in cost of goods sold in the consolidated statements of operations and comprehensive loss.

The Company is also applying an accounting policy election, which allows an entity to exclude from revenue any amounts collected from customers on behalf of third parties, such as sales taxes and other similar taxes the Company collects concurrent with revenue-producing activities. Therefore, revenue is presented net of sales taxes and similar revenue-based taxes.

For incremental costs of obtaining a contract, the Company elected a practical expedient, which permits an entity to recognize incremental costs to obtain a contract as an expense when incurred if the amortization period is less than one year. This election had an immaterial effect on the Company's consolidated financial statements.

Note 9: Income Taxes

The benefit for income taxes includes these components:

	2020	2019
Taxes currently payable	$ (98,508)	$ 25,771
Deferred income taxes	(669,800)	(409,870)
Income tax benefit	$ (768,308)	$ (384,099)

A reconciliation of income tax benefit at the statutory rate to the Company's actual income tax benefit is shown below:

	2020	2019
Computed at the statutory rate - 21%	$ (720,230)	$ (330,200)
Increase (decrease) resulting from		
Goodwill amortization	74,863	74,800
Nondeductible expenses	3,859	4,700
State income taxes	(105,405)	(56,600)
Return to provision	(76,794)	-
Other	55,399	(76,799)
Actual tax benefit	$ (768,308)	$ (384,099)

The tax effects of temporary differences related to deferred taxes shown on the balance sheets were:

	2020	2019
Deferred tax assets		
Allowance for doubtful accounts	$ 6,000	$ 8,900
Inventory overhead costs capitalized for tax purposes	254,200	361,400
Obsolete inventory reserve	242,200	187,600
Accrued expenses	106,300	118,000
Amortization	24,200	16,800
Deferred compensation	4,800	4,800
Interest expense limitation	191,200	-
Other	23,278	1,100
Deferred tax liabilities		
Depreciation	(1,326,600)	(1,500,700)
Prepaids	(49,400)	(52,500)
Goodwill and other intangibles	(3,396,800)	(3,758,800)
Net deferred tax liability	$ (3,920,622)	$ (4,613,400)

Note 10: Employee Benefit Plans

The Company's wholly-owned subsidiary sponsors a defined contribution 401(k) plan that covers substantially all employees. The subsidiary contributes a specified percentage of each participant's annual compensation up to certain limits defined in the 401(k) plan. The subsidiary's charge to expense amounted to approximately $386,000 and $438,000 for the years ended March 31, 2020 and 2019, respectively.

Suprajit USA, Inc.
Notes to Consolidated Financial Statements
March 31, 2020 and 2019

Note 11: Disclosures About Fair Value of Assets and Liabilities

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. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities

Recurring Measurements

The following table presents the fair value measurements of assets and liabilities recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at March 31, 2020 and 2019:

		Fair Value Measurements Using		
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
March 31, 2020				
Liabilities				
Interest rate swap	$ (113,850)	$ -	$ (113,850)	$ -
March 31, 2019				
Liabilities				
Interest rate swap	$ (4,429)	$ -	$ (4,429)	$ -

Interest Rate Swap Agreement

The fair value is estimated using forward-looking interest rate curves and discounted cash flows that are observable or can be corroborated by observable market data and, therefore, are classified within Level 2 of the valuation hierarchy.

Note 12: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

General Litigation

The Company is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have a material adverse effect on the consolidated financial position, results of operations and cash flows of the Company.

Major Customers

Three customers made up approximately 48% and 44% of the Company's total revenue during the years ended March 31, 2020 and 2019, respectively. At March 31, 2020 and 2019, credit extended to these customers was approximately 30% and 24% of accounts receivable, respectively.

Major Supplier

The Company purchases most of its contract labor and rents the facility used for manufacturing at its Juarez, Mexico location from one supplier.

Supplementary Information

Suprajit USA, Inc.
Consolidating Balance Sheet
March 31, 2020

Assets

	Suprajit USA, Inc.	Wescon Controls, LLC	Total	Eliminating Entries	Consolidated
Current Assets					
Cash	$ 1,292,423	$ 520,707	$ 1,813,130	$ -	$ 1,813,130
Accounts receivable	82,616	3,265,172	3,347,788	(82,616)	3,265,172
Inventories	-	7,119,152	7,119,152	-	7,119,152
Prepaid expenses and other	110,384	194,643	305,027	-	305,027
Refundable income taxes	6,615	307,548	314,163	-	314,163
Total current assets	1,492,038	11,407,222	12,899,260	(82,616)	12,816,644
Property and Equipment, at Cost					
Land and land improvements	-	579,766	579,766	-	579,766
Buildings and leasehold improvements	-	2,932,930	2,932,930	-	2,932,930
Machinery and equipment	-	6,248,418	6,248,418	-	6,248,418
Office equipment	-	1,232,721	1,232,721	-	1,232,721
Transportation equipment	-	44,097	44,097	-	44,097
Construction in progress	-	8,838	8,838	-	8,838
	-	11,046,770	11,046,770	-	11,046,770
Less accumulated depreciation and amortization	-	(4,269,544)	(4,269,544)	-	(4,269,544)
	-	6,777,226	6,777,226	-	6,777,226
Other Assets					
Investment in subsidiary	33,680,268	-	33,680,268	(33,680,268)	-
Goodwill	-	10,900,978	10,900,978	-	10,900,978
Indefinite-lived intangible assets	-	1,420,000	1,420,000	-	1,420,000
Definite-lived intangible assets	-	12,114,515	12,114,515	-	12,114,515
	33,680,268	24,435,493	58,115,761	(33,680,268)	24,435,493
Total assets	$ 35,172,306	$ 42,619,941	$ 77,792,247	$ (33,762,884)	$ 44,029,363

Liabilities and Stockholder's Equity

	Suprajit USA, Inc.	Wescon Controls, LLC	Total	Eliminating Entries	Consolidated
Current Liabilities					
Current maturities of long-term debt	$ 6,250,000	$ -	$ 6,250,000	$ -	$ 6,250,000
Line of credit	7,000,000	-	7,000,000	-	7,000,000
Accounts payable	-	3,481,202	3,481,202	-	3,481,202
Payable to parent	-	82,616	82,616	(82,616)	-
Accrued interest	42,025	-	42,025	-	42,025
Accrued salaries, wages and commissions	-	354,643	354,643	-	354,643
Accrued vacation	-	393,552	393,552	-	393,552
Operating lease liability	-	262,338	262,338	-	262,338
Accrued other	-	216,892	216,892	-	216,892
Total current liabilities	13,292,025	4,791,243	18,083,268	(82,616)	18,000,652
Long-term Liabilities					
Long-term debt, less current maturities	2,500,000	(40,592)	2,459,408	-	2,459,408
Interest rate swap agreement	113,850	-	113,850	-	113,850
Deferred income taxes	(47,178)	3,967,800	3,920,622	-	3,920,622
Other long-term liabilities	-	221,222	221,222	-	221,222
Total long-term liabilities	2,566,672	4,148,430	6,715,102	-	6,715,102
Stockholder's Equity					
Preferred stock	-	-	-	-	-
Common stock	1,000	-	1,000	-	1,000
Additional paid-in capital	20,999,000	35,106,584	56,105,584	(35,106,584)	20,999,000
Retained earnings	(1,596,449)	(1,426,316)	(3,022,765)	1,426,316	(1,596,449)
Accumulated other comprehensive loss	(89,942)	-	(89,942)	-	(89,942)
Total stockholder's equity	19,313,609	33,680,268	52,993,877	(33,680,268)	19,313,609
Total liabilities and stockholder's equity	$ 35,172,306	$ 42,619,941	$ 77,792,247	$ (33,762,884)	$ 44,029,363

Suprajit USA, Inc.
Consolidating Statement of Operations and Comprehensive Loss
Year Ended March 31, 2020

	Suprajit USA, Inc.	Wescon Controls, LLC	Total	Eliminating Entries	Consolidated
Net Sales	$ -	$ 37,432,345	$ 37,432,345	$ -	$ 37,432,345
Cost of Goods Sold	-	32,788,944	32,788,944	-	32,788,944
Gross Profit	-	4,643,401	4,643,401	-	4,643,401
Selling, General and Administrative Expenses	54,782	7,186,801	7,241,583	-	7,241,583
Operating Loss	(54,782)	(2,543,400)	(2,598,182)	-	(2,598,182)
Other Expense					
Interest expense	-	(795,595)	(795,595)	-	(795,595)
Other	-	(35,891)	(35,891)	-	(35,891)
	-	(831,486)	(831,486)	-	(831,486)
Loss Before Income Taxes	(54,782)	(3,374,886)	(3,429,668)	-	(3,429,668)
Benefit for Income Taxes	-	(768,308)	(768,308)	-	(768,308)
Net Loss From Subsidiary	(2,606,578)	-	(2,606,578)	2,606,578	-
Net Loss	(2,661,360)	(2,606,578)	(5,267,938)	2,606,578	(2,661,360)
Other Comprehensive Loss					
Change in fair value of rate swap agreement, net of taxes of $(22,978)	(86,443)	-	(86,443)	-	(86,443)
Comprehensive Loss	$ (2,747,803)	$ (2,606,578)	$ (5,354,381)	$ 2,606,578	$ (2,747,803)

Suprajit USA, Inc.
Consolidating Statement of Cash Flows
Year Ended March 31, 2020

	Suprajit USA, Inc.	Wescon Controls, LLC	Total	Eliminating Entries	Consolidated
Operating Activities					
Net loss	$ (2,661,360)	$ (2,606,578)	$ (5,267,938)	$ 2,606,578	$ (2,661,360)
Items not requiring (providing) cash					
Depreciation and amortization	-	4,607,452	4,607,452	-	4,607,452
Amortization of debt issuance costs	-	27,061	27,061	-	27,061
Loss on sale of property and equipment	-	25,342	25,342	-	25,342
Deferred income taxes	(7,400)	(662,400)	(669,800)	-	(669,800)
Equity in loss of subsidiary	2,606,578	-	2,606,578	(2,606,578)	-
Changes in					
Accounts receivable	5,320	716,301	721,621	755	722,376
Inventories	-	3,414,124	3,414,124	-	3,414,124
Related party receivables/payables	-	(5,320)	(5,320)	(755)	(6,075)
Prepaid expenses and other	45,208	20,301	65,509	-	65,509
Income tax refundable	7,400	(96,017)	(88,617)	-	(88,617)
Accounts payable	-	(1,503,373)	(1,503,373)	-	(1,503,373)
Operating lease liability	-	(349,784)	(349,784)	-	(349,784)
Accrued liabilities	(39,836)	(72,848)	(112,684)	-	(112,684)
Net cash provided by (used in) operating activities	(44,090)	3,514,261	3,470,171	-	3,470,171
Investing Activities					
Purchase of property and equipment	-	(217,340)	(217,340)	-	(217,340)
Net cash used in investing activities	-	(217,340)	(217,340)	-	(217,340)
Financing Activities					
Borrowings under line-of-credit agreement	9,479,000	-	9,479,000	-	9,479,000
Payments under line-of-credit agreement	(7,299,000)	-	(7,299,000)	-	(7,299,000)
Principal payments on long-term debt	(5,000,000)	-	(5,000,000)	-	(5,000,000)
Return of capital (paid) received from subsidiary	2,819,994	(2,819,994)	-	-	-
Net cash used in financing activities	(6)	(2,819,994)	(2,820,000)	-	(2,820,000)
Increase (Decrease) in Cash	(44,096)	476,927	432,831	-	432,831
Cash, Beginning of Year	1,336,519	43,780	1,380,299	-	1,380,299
Cash, End of Year	$ 1,292,423	$ 520,707	$ 1,813,130	$ -	$ 1,813,130