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REC'D WAS APR 29 1975

TO: CLYDE S CARTER, ESQ
SENIOR VICE PRESIDENT
AIR AMERICA, INC.

CC: K M SMITH

RE: (A) CONTRACT FOR SALE OF SHARES DATED AUGUST 21, 1974
(B) CLOSING AUDIT AS OF JANUARY 31, 1975

YOUR TELEX CONCERNING THE ABOVE SUBJECTS WAS RECEIVED ON APRIL 28, 1975. E-SYSTEMS WILL BE PLEASED TO SET A TIME FOR A MEETING AT OUR MUTUAL CONVENIENCE TO DISCUSS OUR EXCEPTIONS TO THE JANUARY 31, 1975 AUDIT REPORT ("AUDIT REPORT") PREPARED BY COOPERS AND LYBRAND ("C AND L") WHICH WAS FORWARDED TO US EARLIER BY YOUR OFFICE AND TO DISCUSS ANY OTHER ITEMS OF MUTUAL INTEREST. WE CONTEMPLATE THAT MR SMITH WILL REPRESENT E-SYSTEMS AT THIS MEETING AND HE WOULD PREFER THAT MR VELTE BE IN ATTENDANCE. IN THAT CONNECTION, CAN YOU ADVISE WHEN MR VELTE WOULD BE AVAILABLE SO THAT THE MEETING CAN BE ARRANGED?

THE AUDIT REPORT REFLECTS, ON PAGE 6, THAT THE NET ASSET VALUE OF AIR ASIA AS OF JANUARY 31, 1975 IS ~~U.S.\$3,391,412~~ ABOVE THE COMPANY'S NET BOOK VALUE OF U.S.\$3,218,000 ON WHICH THE SALE AND PURCHASE OF AACL WAS PREDICATED. E-SYSTEMS DISAGREES WITH THIS STATEMENT OF C AND L AND BELIEVES THAT THE NET BOOK VALUE OF AACL ABOVE THE U.S.\$3,218,000 SHOULD BE U.S.\$63,448. EACH ADJUSTMENT NECESSARY TO MAKE THE CLOSING AUDIT ACCURATELY REFLECT THE ASSETS AND LIABILITY OF AIR ASIA AS OF JANUARY 31, 1975, CONSISTENT WITH THE AGREEMENT FOR SALE OF SHARES AND THE MEMORANDA AGREEMENTS OF OCTOBER 4, 1974, NOVEMBER 15, 1974, AND JANUARY 24, 1975 AS FOLLOWS:

1. AACL INVENTORY AT SAIGON.

THE CLOSING AUDIT STATEMENT REFLECTS INVENTORY OF AACL IN THE POSSESSION OF AAM WHICH IS SUBJECT TO A SAFEGUARDING AGREEMENT PURSUANT TO THE MEMORANDUM DATED OCTOBER 4, 1974. IN VIEW OF THE WAR IN SOUTH VIETNAM, THIS INVENTORY WILL NOT BE RECOVERED AND THESE ASSETS SHOULD HAVE BEEN WRITTEN OFF THE BOOKS OF AIR ASIA. THE TOTAL AMOUNT OF THIS ADJUSTMENT IS U.S.\$110,537.

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327,964

2. LANDING COSTS INCLUDED IN JANUARY 31, 1975 INVENTORY.

AT JANUARY 31, 1975, CERTAIN LANDING COSTS IN THE AMOUNT OF U.S.\$56,949, WHICH, ACCORDING TO AACL'S PRIOR PRACTICE AS OF MARCH 31, 1974 AND PRIOR PERIODS, WOULD HAVE BEEN CHARGED TO AAM, WERE IN FACT INCLUDED IN THE AUDIT REPORT AS ASSETS OF AACL. THIS REPRESENTS A CHANGE IN ACCOUNTING PRINCIPLES AT THE TIME OF THE CLOSING AUDIT AND THEREFORE IS IN VIOLATION OF THE "CONSISTENCY STANDARD" OF THE ACCOUNTING PRACTICES AGREED TO BY THE PARTIES IN THE AGREEMENT FOR SALE OF SHARES. THE AMOUNT OF THIS ADJUSTMENT IS U.S.\$56,949.

3. AMORTIZATION OF BUILDING COSTS ON LEASED LAND AT NORTH HOLLYWOOD.

AACL'S ACCOUNTING MANUAL PROVIDES THAT BUILDING COSTS ON LEASED PROPERTY ARE TO BE AMORTIZED OVER THE LIFE OF THE ORIGINAL LEASE. AACL EARLIER CARRIED CERTAIN BUILDING COSTS ASSOCIATED WITH THE NORTH HOLLYWOOD PROPERTY ON ITS BOOKS BEYOND THE ORIGINAL LIFE OF THE LEASE. THIS ERROR WAS DISCOVERED IN DECEMBER OF 1974 AND AN ADJUSTMENT WAS MADE TO THE BOOKS OF AACL, WRITING OFF THIS COST. HOWEVER, THIS ENTRY WAS REVERSED SETTING UP THE COST TO BE AMORTIZED IN THE FUTURE. GENERALLY ACCEPTED ACCOUNTING PRINCIPLES DO REQUIRE THAT WHERE AN ERROR IS MADE IN THE BOOKS THAT THE ERROR BE CORRECTED. THE FORCE AND EFFECT OF THIS CHANGE IS TO CARRY FORWARD THE ERROR AFTER THE CLOSING AUDIT DATE. THE AMOUNT OF THIS ADJUSTMENT IS U.S.\$13,636.

4. COSTS RELATED TO IBM SYSTEM 3 DISC PACKS.

AACL PURCHASED 10 OF THESE DISC PACKS. THE UNIT PRICE FOR EACH PACK WAS UNDER U.S.\$250. ACCORDING TO AACL'S ACCOUNTING POLICY, ITEMS PURCHASED WHICH HAVE VALUE OF U.S.\$250 OR LESS ARE EXPENSED AND NOT CAPITALIZED. THE AUDIT STATEMENT REFLECTS THE CAPITALIZATION RATHER THAN THE EXPENSE OF THESE ITEMS, WHICH IS INCONSISTENT WITH AACL'S ACCOUNTING POLICY. THE AMOUNT OF THIS ADJUSTMENT IS U.S.\$2,200.

5. WORK-IN-PROCESS INVENTORY ADJUSTMENT RELATING TO INDIVIDUAL ACCOUNTS RECEIVABLE.

THE WORK-IN-PROCESS CONTAINS U.S.\$811 OF WORK-IN-PROCESS RELATED TO TRI-9 AIRLINES LOCATED IN PHNOM PENH, KHMER. THIS COMPANY HAS IN ALL PROBABILITY FAILED BY REASON OF THE TAKE-OVER OF CAMBODIA BY THE KHMER ROUGE AND THE ACCOUNTS SHOULD, ACCORDING TO GENERALLY ACCEPTED ACCOUNTING PRINCIPLES, HAVE BEEN WRITTEN OFF. THE TOTAL AMOUNT OF THIS ADJUSTMENT IS U.S.\$811.

6. VOCATIONAL TRAINING FUND LIABILITY.

THIS LIABILITY IS A TAX ON AACL BY THE ROC. THIS LIABILITY WAS TRANSFERRED FROM AACL TO AAM. SUCH TRANSFER CAUSES THE BALANCE SHEET OF AACL NOT TO ACCURATELY REFLECT ITS LIABILITIES. THIS LIABILITY SHOULD REMAIN WITH AACL. THE TOTAL AMOUNT OF ADJUSTMENT IS U.S.\$43,683.

7. RECORDING OF PREPAID INSURANCE.

LISTED ON AACL'S STATEMENT DATED JANUARY 31, 1975 WAS PREPAID INSURANCE FOR FIDELITY BONDS AND THE POLICY FOR FIRE AND ALLIED RISKS. THESE TWO POLICIES WERE CANCELLED AS OF JANUARY 31, 1975 BY AAM; THEREFORE, THESE ITEMS WERE NO LONGER AN ASSET AS OF THAT DATE AND SHOULD HAVE BEEN EXPENSED. TOTAL AMOUNT OF THIS ADJUSTMENT IS U.S.\$8,624.

8. CORPORATE INCOME TAXES.

IN ACCRUING THE AMOUNT OF CORPORATE INCOME TAXES TO BE PAID BY AACL FOR THE PERIOD OF APRIL 1, 1974 THROUGH JANUARY 31, 1975, THE AMOUNT OF TAX LIABILITY WAS REDUCED BY U.S.\$67,000 REPRESENTING A TAX LOSS CARRYFORWARD. THERE IS NO PROVISION IN THE ROC LAW PERMITTING EITHER A TAX LOSS CARRYFORWARD OR A TAX LOSS CARRYBACK. THIS LIABILITY SHOULD BE CARRIED ON THE BOOKS OF AACL AS OF JANUARY 31, 1975 IN ORDER TO ACCURATELY REFLECT THE TAX LIABILITY OF AACL. TOTAL AMOUNT OF THIS ADJUSTMENT IS U.S. \$67,000.

9. CORPORATE INCOME TAXES.

THE AMOUNT OF CORPORATE TAX LIABILITY ACCRUED ON THE BOOKS OF AACL FROM APRIL 1, 1974 THROUGH JANUARY 31, 1975 HAS BEEN UNDERSTATED BY THE AMOUNT OF U.S.\$24,525. THIS AMOUNT REPRESENTS THE TAX ON THE DIFFERENCE BETWEEN THE AMOUNT OF DEDUCTION TAKEN FOR RETIREMENT PAY AND THE AMOUNT PERMITTED BY THE ROC TAX LAWS. THE ROC ONLY PERMITS A DEDUCTION FOR ACTUAL PAYMENTS AND NOT FOR ACCRUALS. THE TAX LIABILITY FOR AACL IS THEREFORE NOT ACCURATELY REFLECTED IN THE JANUARY 31 STATEMENT. TOTAL AMOUNT OF THIS ADJUSTMENT AT A 25 PERCENT TAX RATE IS U.S.\$24,525.

WITH RESPECT TO ITEMS 8 AND 9, C AND L HAVE EXPRESSLY QUALIFIED THEIR OPINION WITH RESPECT TO THE CLAIMING OF THESE DEDUCTIONS. C AND L NOTES THAT THE COMPANY'S STATEMENT OF ASSETS AND LIABILITIES AS OF MARCH 31, 1974 DID INCLUDE PROVISIONS FOR POSSIBLE DISALLOWANCES UPON EXAMINATION OF ITS RETURNS. NO PROVISIONS WERE MADE FOR THESE POSSIBLE DISALLOWANCES, THEREFORE, THE STATEMENT OF JANUARY 31, 1975 IS INCONSISTENT WITH THE ACCOUNTING PRINCIPLES UTILIZED IN THE PREPARATION OF AACL'S STATEMENT AS OF MARCH 31, 1974 AND AS A CONSEQUENCE IS INCONSISTENT WITH THE PROVISIONS OF THE AGREEMENT FOR SALE OF SHARES. ACCORDINGLY, THE STATEMENT OF AACL MUST REFLECT PROVISIONS FOR POSSIBLE DISALLOWANCES IN ORDER TO BE CONSISTENT WITH ITS STATEMENT AS OF MARCH 31, 1974.

TOTAL AMOUNT OF ADJUSTMENTS (ITEMS 1 - 9)	\$ 327,965
TOTAL NET BOOK VALUE OF AACL (ADJUSTED)	3,281,448
LESS NET BOOK VALUE PER AGREEMENT	3,218,000
EXCESS OF NET BOOK VALUE DUE AAM	\$ 63,448

PAGE 4 OF THE AUDIT STATEMENT REFLECTS ACCOUNTS RECEIVABLE LEFT WITH AACL AS FOLLOWS:

U. S. GOVERNMENT	\$ 758,088
OTHER CUSTOMERS	654,858
COMPANY PERSONNEL	10,806

	\$1,418,752

EXCEPT FOR THE CATEGORY OF COMPANY PERSONNEL, THE MEETING BETWEEN ESY AND AAM IS EXPECTED TO MAKE THE DETERMINATION OF THE COLLECTABILITY OF THESE ACCOUNTS RECEIVABLE IN ACCORDANCE WITH THE AGREEMENTS. IN ADDITION, THE AMOUNT OF ACCOUNTS RECEIVABLE LEFT WITH AACL BY AAM IN THE CATEGORY OF "OTHER CUSTOMERS" IS IN EXCESS OF THE AMOUNT CONTEMPLATED BY THE AGREEMENT FOR SALE OF SHARES AND THE MEMORANDUM DATED JANUARY 24, 1975.

THE ABOVE ITEMS ARE EXPECTED TO BE ON THE AGENDA YOU PROPOSED, INCLUDING SUCH OTHER ITEMS THAT AAM WISHES TO PROPOSE IN THIS CONNECTION. PLEASE ADVISE WHAT ITEMS OTHER THAN THE ABOVE AAM WISHES TO DISCUSS. SHOULD YOU HAVE ANY QUESTIONS IN THE INTERIM, PLEASE CONTACT THE UNDERSIGNED OR MR BOLDING OF MY OFFICE.

VERY TRULY YOURS,

JAMES W CROWLEY
VICE PRESIDENT AND
GENERAL COUNSEL

APRIL 29, 1975

END

COR. ITEM 9, 2ND PAR, LINE 6, LAST 2 WORDS SHOULD READ:

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