

EXHIBIT 7
Convertible Debt Issued With Warrants

Company E issues \$1 million of three-year notes payable to investors. The investors are also given an aggregate of 10,000 warrants to purchase Company E's common stock at \$5 per share (the market price as of the date of issuance). The allocated fair value of the warrants based on the Black-Scholes formula is \$200,000. The notes are convertible into Company E's common stock at \$4 per share. As discussed below, both the warrants and conversion feature will be accounted for as equity. Company E is not subject to any registration payment penalty.

First, the \$1 million cash proceeds are allocated between the debt and the warrants based on their relative fair values:

Cash	\$1,000,000	
Notes Payable		\$800,000
Additional Paid-in Capital		\$200,000

Second, the beneficial conversion feature is calculated:

Number of shares to be issued if the entire note is converted (\$1,000,000/\$4 per share): 250,000

Effective conversion price based on the proceeds of \$800,000 allocated to the convertible debt (\$800,000/250,000 shares): \$3.20

Intrinsic value per share (\$5 market value less \$3.20 effective conversion price): \$1.80

Total value of beneficial conversion (250,000 shares at \$1.80): \$450,000

The value of the beneficial conversion feature is recorded as a further discount on the debt with a corresponding credit to capital:

Notes Payable	\$450,000
Additional Paid-in Capital	\$450,000

The notes now have a \$650,000 discount that will be amortized to interest expense.

For further guidance on this calculation, refer to EITF 00-27, Issue 1 (paragraphs 5-7) and EITF 98-5.