



## Consolidated Financial Report for the Nine Months Ended September 30, 2004 (Unaudited)

**AnGes MG, Inc.** <http://www.anges-mg.com>

Listings: Mothers of the Tokyo Stock Exchange, Code 4563

Head Office: 4F, Saito Bio-Incubator, 7-7-15, Saito-Asagi, Ibaraki, Osaka, 567-0085, Japan

Adoption of the U.S.GAAP: None

### 1. Business Results for the Third Quarter 2004 (From Jan. 1, 2004 to Sep. 30, 2004)

#### (1) Results of Operations (Figures are rounded down to the nearest million yen)

	Revenues		Operating loss		Ordinary loss	
	Million yen	%	Million yen	%	Million yen	%
3Q 2004 (9 Months)	1,760	5.0	(1,042)	-	(1,033)	-
3Q 2003 (9 Months)	1,677	-	(843)	-	(818)	-
FY 2003 (12 Months)	2,453		(948)		(953)	

	Net loss		Net loss per share	Diluted net loss per share
	Million yen	%	yen	Yen
3Q 2004 (9 Months)	(969)	-	(10,178.24)	-
3Q 2003 (9 Months)	(815)	-	(9,670.04)	-
FY 2003 (12 Months)	(978)		(11,300.35)	-

Notes) 1. Equity in net income of unconsolidated subsidiaries and affiliates

3Q 2004: - million yen    3Q 2003: - million yen    Fiscal year 2003: - million yen

2. Average number of shares issued during the period ended (consolidated)

3Q 2004: 95,293 shares    3Q 2003: 84,363 shares    Fiscal year 2003: 86,585 shares

3. Change in accounting policies: None

4. Percentages for Revenues, Operating loss, Ordinary loss and Net loss indicate changes from the previous term.

#### (2) Financial Position

	Total assets	Shareholders' equity	Shareholders' equity ratio	Shareholders' equity per share
	Million yen	Million yen	%	Yen
Sep. 30, 2004	11,371	9,114	80.2	93,866.17
Sep. 30, 2003	5,178	3,711	71.7	43,598.34
Dec. 31, 2003	10,974	9,454	86.2	100,670.11

Notes) 1. Number of shares issued at end of period (consolidated)

Sep. 30, 2004: 97,100 shares    Sep. 30, 2003: 85,134 shares    Dec. 31, 2003: 93,914 shares

#### (3) Cash Flows

	Cash flows from operating activities	Cash flows from investing activities	Cash flows from financing activities	Cash and cash equivalents, at end
	Million yen	Million yen	Million yen	Million yen
3Q 2004 (9 Months)	(1,128)	(94)	781	4,139
3Q 2003 (9 Months)	(759)	(153)	54	2,974
FY 2003 (12 Months)	(689)	(4,484)	5,927	4,572

#### (4) Scope of consolidation and application of the equity method

Number of consolidated subsidiaries: 3

Number of non-consolidated subsidiaries accounted for under the equity method: N/A

Number of affiliates accounted for under the equity method: N/A

#### (5) Changes in the scope of consolidation and application of the equity method

Number of consolidated subsidiaries: Increase N/A    Decrease N/A

Number of affiliates accounted for under the equity method: Increase N/A    Decrease N/A

### 2. Earnings Forecast for the Fiscal Year 2004 (From Jan. 1, 2004 to Dec. 31, 2004)

	Revenues	Ordinary loss	Net loss
	Million yen	Million yen	Million yen
Full-year	2,000-3,000	(1,900)-(900)	(1,900)-(900)

*\*Since descriptions about future events, for instance, earnings forecast for FY 2004, are estimation, results may differ from this estimation due to changes of several economic conditions.*

*\*\*This financial report has been translated from Japanese 3Q Report which has been prepared in accordance with generally accepted accounting principles in Japan, for reference purposes only. Also some changes are added to this report in order to present in a form more familiar to the readers outside Japan.*

## **AnGes MG, Inc.**

### **Operational and financial results for the nine months ended September 30, 2004**

#### **1. Overview**

Supported by business investment and exports, the Japanese economy continues recovering steadily. Exports to Asia, mainly of machinery equipment to China, have increased and business investment is increasing due to an improvement of corporate profits and progress in capital stock adjustment while the unemployment rate still remains at high level. As for short-term prospects, the economic recovery in Japan is expected to continue as the world economy recovers.

The pharmaceutical industry in Japan faces an ever-increasing challenge to develop innovative products, which can be accepted in the global market while the domestic market could be reduced based on the government policy to control healthcare cost and is exposed to offensive of foreign company.

For the nine months ended September 30, 2004, AnGes has made steady progress in product development and initiated negotiations to establish alliances and partnerships.

For the nine months ended September 30, 2004, total revenue has increased by 5.0% to reach ¥1,760 Million. Pre-clinical and/or clinical studies have been conducted for HGF and NF-κB decoy oligonucleotide. AnGes has licensed and/or joint R&D agreements with Daiichi Pharmaceutical Co., Ltd., Seikagaku Corporation and Goodman Co., Ltd., from which AnGes received a R&D support payment. These payments are accounted for as operating revenues.

Regarding the reagents business, AnGes has a license agreement on HVJ-E vector with Ishihara Sangyo Kaisha, Ltd. and is entitled to receive royalties from them. In addition to Ishihara Sangyo, AnGes has non-exclusive license agreements on NF-κB decoy with two bio ventures, Gene Design Inc. and Hokkaido System Science Co., Ltd. AnGes is entitled to receive royalty payments from these agreements.

The following is a summary of the financial results of the AnGes group companies by business segments for the nine months ended September 30, 2003 and 2004, and for the year ended December 31, 2003.

<Segment information (In millions)>

Business	9 months ended September 30,				Year ended December 31,	
	2004		2003		2003	
	Revenue	(%)	Revenue	(%)	Revenue	(%)
Pharmaceuticals.....	¥ 1,672	95.0	¥ 1,565	93.3	¥ 2,335	95.2
Reagents.....	3	0.2	2	0.1	3	0.1
Other.....	84	4.8	109	6.6	114	4.7
	<u>¥1,760</u>	<u>100.0</u>	<u>¥ 1,677</u>	<u>100.0</u>	<u>¥ 2,453</u>	<u>100.0</u>

As a result, for the nine months ended September 30, 2004, ordinary loss was ¥1,033 Million compared to loss of ¥818 Million in the third quarter of 2003. The ordinary loss is widened mainly due to the increase in R&D expenses to be borne by AnGes.

For the nine months ended September 30, 2004 net loss was ¥969 Million compared to loss of ¥815 Million in the third quarter of 2003. Extraordinary gain was recorded due to issuance of common stock by the subsidiary, GenomIdea.

## 2. Cash flows (In millions)

For the nine months ended September 30, 2004, cash and cash equivalents decreased by ¥432 Million compared to the decrease of ¥ 855 Million in the third quarter of 2003. As of September 30 2004, cash and cash equivalents was ¥4,139 Million.

### (Cash flows from operating activities)

For the nine months ended September 30, 2004, cash flows from operating activities decreased by ¥1,128 Million compared to the decrease of ¥759 Million in the third quarter of 2003. This is the result of net loss (¥972 Million), depreciation and amortization (¥90 Million), increase in advances (¥326 Million) and increase in customer advances (¥141 Million).

### (Cash flows from investing activities)

For the nine months ended September 30, 2004, cash flows from investing activities decreased by ¥94 Million compared to the decrease of ¥153 Million in the third quarter of 2003. Capital investment was mainly for our Head office and laboratory which was relocated on September 1, 2004, HGF Patent and Information Technology for the clinical development. Purchases of property and equipment of ¥136 Million and Purchase of intangible assets of ¥143 Million were recorded, whereas proceeds from sale of marketable securities of ¥200 Million was recorded, which was purchased by floating money last year.

(Cash flows from financing activities)

For the nine months ended September 30, 2004, cash flows from financing activities increased by ¥781 Million compared to the increase of ¥54 Million in the third quarter of 2003. The increase comes from the exercising of employee stock options of ¥620 Million and Proceeds from issuance of common stock to minority shareholders of ¥161 Million.

### **3. Research and Development**

For the nine months ended September 30, 2004, R&D expenses have increased by 13.7% over the previous term to reach ¥ 2,358 Million. The ratio of R&D expenses to operating revenue reached to 134.0%.

#### **<Major developments>**

For HGF development, clinical development programs for PAD (Peripheral Arterial Disease) and IHD (Ischemic Heart Disease) have been advanced in Japan and US. Regarding PAD, while Phase II clinical trial studies started in US in April, 2003, Phase III clinical studies also started in Japan. The IND for the US IHD Phase I clinical trial was submitted to the FDA for review in February 2004 and it was cleared in July 2004. The US IHD Phase I clinical trial studies will be started in the near future. AnGes was also in the preparation for IND of IHD clinical trial in Japan. According to the clinical statistics, there are more than millions of patients who suffer ischemic heart disease and lack of effective medicines for the treatment. The Phase I clinical trial of IHD in the US will be a very significant development milestone for the HGF project.

AnGes signed an exclusive licensing agreement with NeoChemir Inc. (hereinafter "NeoChemir") to distribute their new carbon dioxide generating wound dressing for the Japanese market, in June 2004. The dioxide generating wound dressing patent was filed by NeoChemir. The goal of this joint development is to use the HGF plasmid as the treatment for the patients with ischemic skin ulcers. The introduction at this time of this new wound dressing for the treatment of ischemic ulcers and other diseases is expected to reinforce our product lineup, and help us continue to address the needs of the medical industry in the field of ischemic diseases

The pre-clinical studies including efficacy, toxicology and stability, for NF-κB decoy oligonucleotide have been conducting for NF-κB decoy nucleotide to verify safety, stability and characterization of pharmacological properties of the agents supporting the possible indications of Atopic dermatitis, psoriasis, rheumatic arthritis, and (degenerative) osteoarthritis. Preparations to initiate the clinical trials in Japan are in progress.

In order to effectively deliver the NF-κB decoy oligonucleotide for new applications, AnGes is actively working with drug delivery industry leaders to develop an effective administration. In June 2004, AnGes and Shimadzu Corporation signed a joint research agreement to use Shimadzu's "Shima JET" needleless hypodermic pressure injector for NF-κB decoy oligonucleotide for the

application of treating patients with psoriasis.

AnGes initiated a joint development with Gene Design Inc to develop the next-generation decoy nucleotides. Nucleotide is not suitable to be administered intravenously because it is relatively easily broken down by the nuclease in blood. So, its use is limited to diseases for which topical administrations or local administrations are possible. In this joint development, AnGes is aiming to develop the next-generation decoy nucleotides to be easily administered intravenously or orally for treating either cancers or Inflammatory Bowel disease (IBD).

**<R&D projects and its current status>**

Project	Target indications	Region	Development stage	Alliance partners
HGF	PAD	Japan	Phase III clinical trials	Daiichi Pharmaceutical
		US	Phase II clinical trials	
	IHD	US	Preparing for Phase I clinical trials (IND Cleared)	
	Parkinson disease		Pre-clinical trials	Yet to be decided
NF-κB decoy oligonucleotide	Atopic dermatitis		Preparing for clinical trials	Yet to be decided
	Psoriasis		Pre-clinical trials	Yet to be decided
	Rheumatic arthritis		Preparing for clinical trials	Seikagaku Corporation
	Degenerative osteoarthritis		Pre-clinical trials	
	Prevention of restenosis		Preparing for clinical trials	Goodman

HVJ-E vector technologies have been developed by its subsidiary, GenomIdea, Inc. GenomIdea developed the device for a DNA-screening technology together with Prof. Kaneda of University of Osaka Medical School and National Institute of Advanced Industrial Science and Technology (AIST) Kansai. GenomIdea initiated research of discovery of a new DNA candidate for drug development using HVJ-E. The drug design system for next-generation nucleic acid medicines (siRNA) has been developed with collaborations with Osaka University, AIST Kansai and Mitsubishi Space Software Co., Ltd.

Process & assay development and manufacturing of HVJ-E has been advanced by using the cell culture in stirred tank bioreactor and a scalable purification process. The development will enable using HVJ-E for future therapeutic applications such as cancer and vaccine. Lately, the GMP Master cell bank has been successfully manufactured, and the final release is completed. The preparation of GMP Virus Bank is also in progress.

#### 4. Outlook for 2004

We aim to make further progress in the current major projects and establish an alliance with new partners to increase revenues including license payments. The financial outlook depends upon uncertain factors such as progress of the current R&D project proceeds and the contract negotiations with new partnering companies. The projected revenue and income for the year ending December 31, 2004 are as follows;

< Consolidated basis >

Revenue.....	¥ 2,000 ~ ¥ 3,000 Million
Ordinary income/ (loss).....	¥ (1,900) ~ ¥ (900) Million
Net income / (loss).....	¥ (1,900) ~ ¥ (900) Million

*\*Since descriptions about future events, for instance, earnings forecast for FY 2004, are estimation, results may differ from this estimation due to changes of several economic conditions.*

**AnGes MG, Inc**  
**Consolidated Balance Sheets**  
(In thousands)  
(Unaudited)

	September 30,		December 31,
	2004	2003	2003
<b>Assets</b>			
Current assets:			
Cash and bank deposits.....	¥ 5,639,637	¥ 2,974,334	¥ 6,072,021
Marketable securities.....	2,600,321	—	2,298,748
Beneficial interest in trust.....	500,000	—	500,000
Accounts receivable.....	154,822	117,517	84,765
Inventories.....	494,610	513,745	530,167
Advances.....	1,261,735	1,080,461	935,523
Other current assets.....	145,821	94,640	175,007
Allowance for doubtful accounts.....	—	(416)	(116)
Total current assets.....	10,796,947	4,780,282	10,596,116
Property and equipment, net.....	277,360	223,025	198,059
Goodwill, net.....	13,608	21,432	20,361
Other intangible assets, net.....	224,949	99,911	106,094
Other assets.....	59,023	54,233	53,492
Total assets.....	¥ 11,371,890	¥ 5,178,886	¥ 10,974,124
<b>Liabilities and Stockholders' equity</b>			
Current liabilities:			
Accounts payable.....	150,586	222,844	107,939
Accrued liabilities.....	568,130	99,145	106,146
Customer advances.....	1,414,561	1,116,088	1,272,617
Other current liabilities.....	7,759	7,967	7,049
Total current liabilities.....	2,141,038	1,446,046	1,493,753
Minority interest.....	116,446	21,139	26,037
Stockholders' equity:			
Common stock.....	5,096,806	1,829,672	4,784,341
Capital surplus.....	6,394,199	3,127,065	6,081,734
Accumulated deficit.....	(2,369,053)	(1,236,490)	(1,399,134)
Unrealized gains (losses) on securities.....	233	—	(1,957)
Foreign currency translation adjustments.....	(7,781)	(8,546)	(10,651)
Total stockholders' equity.....	9,114,405	3,711,700	9,454,332
Total liabilities and stockholders' equity.....	¥ 11,371,890	¥ 5,178,886	¥ 10,974,124

\*See accompanying notes.

**AnGes MG, Inc**  
**Consolidated Statements of Operations**  
(In thousands, except per share data)  
(Unaudited)

	9 months ended September 30,		Year ended December 31,
	2004	2003	2003
<b>Operating revenues</b> .....	¥ 1,760,842	¥ 1,677,394	¥ 2,453,440
<b>Operating expenses:</b>			
Research and development.....	2,358,848	2,075,208	2,807,757
Selling, general and administrative.....	444,308	446,018	593,962
Total operating expenses.....	2,803,156	2,521,226	3,401,719
Operating loss.....	(1,042,314)	(843,831)	(948,278)
<b>Non-operating income (expenses):</b>			
Interest income.....	4,379	143	605
Grant.....	1,972	19,929	19,929
Foreign currency transaction gain, net.....	4,023	6,129	9,502
Stock issuance cost.....	(5,639)	(181)	(35,925)
Other items, net.....	3,740	(480)	218
Ordinary loss.....	(1,033,837)	(818,290)	(953,947)
<b>Extraordinary gain (loss):</b>			
Reversal of allowance for doubtful accounts, net...	116	—	224
Gain on change in holding ratio of subsidiary.....	62,850	—	—
Loss on write-down of advances.....	—	—	(24,541)
Loss on dispositions of property and equipment and intangible assets.....	(1,334)	—	(188)
Loss before income taxes and minority interest.....	(972,205)	(818,290)	(978,452)
Provision for Income taxes – Current.....	3,416	5,975	4,571
Deferred.....	—	528	(482)
Minority interest loss.....	5,702	8,999	4,100
Net loss.....	¥ (969,918)	¥ (815,796)	¥ (978,440)
<b>Loss per share:</b>			
Basic.....	¥ (10,178.24)	¥ (9,670.04)	¥ (11,300.35)
Diluted.....	—	—	—
<b>Shares used in calculation of loss per share data:</b>			
Basic.....	95,293	84,363	86,585
Diluted.....	—	—	—

\*See accompanying notes.

\*\*Diluted loss per share data is not calculated because the impact was anti-dilutive.



**AnGes MG, Inc**  
**Consolidated Statements of Capital surplus and Accumulated Deficit**  
(In thousands)  
(Unaudited)

	9 months ended September 30,		Year ended December 31,
	2004	2003	2003
<b>Capital surplus:</b>			
Balance at beginning of period.....	¥ 6,081,734	¥ 3,099,940	¥ 3,099,940
Issuance of common stock upon public offering.....	—	—	2,930,147
Issuance of common stock upon exercise of stock options.....	312,465	27,125	51,647
Balance at end of period.....	6,394,199	3,127,065	6,081,734
<b>Accumulated deficit:</b>			
Balance at beginning of period.....	(1,399,134)	(420,693)	(420,693)
Net loss.....	(969,918)	(815,796)	(978,440)
Balance at end of period.....	¥ (2,369,053)	¥ (1,236,490)	¥ (1,399,134)

\*See accompanying notes.

**AnGes MG, Inc**  
**Consolidated Statements of Cash Flows**  
(In thousands)  
(Unaudited)

	9 months ended September 30,		Year ended
	2004	2003	December 31, 2003
<b>Cash flows from operating activities:</b>			
Loss before income taxes and minority interest.....	¥ (972,205)	¥ (818,290)	¥ (978,452)
Depreciation and amortization.....	90,677	97,889	138,084
Amortization of goodwill.....	3,214	—	1,071
(Decrease) Increase in allowance for doubtful accounts.....	(116)	75	(224)
Interest income.....	(4,379)	(143)	(605)
Foreign currency transaction (gain) loss, net.....	(6,142)	(7,541)	6,296
Loss on dispositions of property and equipment and intangible assets.....	1,334	—	188
Stock issuance cost.....	5,639	181	35,925
Gain on change in holding ratio of subsidiary.....	(62,850)	—	—
(Increase) Decrease in accounts receivable.....	(70,056)	40,431	73,183
Decrease in inventories.....	35,557	284,402	267,980
Increase in other current assets.....	(287,163)	(664,539)	(599,450)
Increase (Decrease) in accounts payable.....	42,647	27,181	(87,723)
Increase in other current liabilities.....	97,354	282,385	456,136
Subtotal.....	(1,126,488)	(757,968)	(687,589)
Interest income received.....	2,793	143	234
Income taxes paid.....	(4,627)	(1,721)	(1,707)
Net cash used in operating activities.....	(1,128,322)	(759,545)	(689,062)
<b>Cash flows from investing activities:</b>			
Increase in time deposit (over 3 months).....	—	—	(1,500,000)
Purchases of marketable securities.....	—	—	(2,300,845)
Proceeds from sales of marketable securities.....	200,000	—	—
Purchase of beneficial interest in trust.....	—	—	(500,000)
Purchases of property and equipment.....	(136,862)	(122,545)	(141,791)
Purchases of intangible assets.....	(143,834)	(21,937)	(32,944)
Purchase of investments in securities.....	—	—	(1,000)
Increase in long-term prepaid expense.....	(15,297)	(6,765)	(6,765)
Proceeds from security deposits received.....	1,807	0	778
Payment for security deposits.....	(300)	(2,178)	(2,222)
Net cash used in investing activities.....	(94,487)	(153,426)	(4,484,790)
<b>Cash flows from financing activities:</b>			
Net proceeds from issuance of common stock.....	620,471	54,068	5,927,663
Net proceeds from issuance of common stock to minority shareholders.....	161,319	—	—
Net cash provided by financing activities.....	781,790	54,068	5,927,663
Effect of exchange rate changes on cash and cash equivalents.....	8,633	3,729	(11,296)
Net (decrease) increase in cash and cash equivalents.....	(432,384)	(855,174)	742,513
Cash and cash equivalents at beginning of period.....	4,572,021	3,829,508	3,829,508
Cash and cash equivalents at end of period.....	¥ 4,139,637	¥ 2,974,334	¥ 4,572,021

\*See accompanying notes.

**AnGes MG, Inc**  
**Notes to Consolidated Financial Statements (Unaudited)**  
**September 30, 2004**

**1. Basis of presenting consolidated financial statements**

The accompanying consolidated financial statements of AnGes MG, Inc (“AnGes”) and its consolidated subsidiaries (collectively, the “Company”) are basically an English version of those which have been prepared in accordance with generally accepted accounting principles in Japan and filed with the Tokyo Stock Exchange as “3rd Quarter financial report.”

The accompanying consolidated financial statements incorporate certain reclassifications of figures from those included in the 3rd Quarter financial report in order to present in a form more familiar to the readers outside Japan. Certain amounts in the accompanying consolidated financial statements from prior year have been reclassified to conform to the current year presentation. In addition, the notes to consolidated financial statements included certain information which is not required under Japan GAAP but is presented herein as additional information.

The amounts presented in the consolidated financial statements are rounded down to the nearest thousand yen.

**2. Summary of Significant Accounting Policies**

***Principles of Consolidation***

The consolidated financial statements include the accounts of AnGes and its subsidiaries in which AnGes has a controlling financial interest and exercise control over its operation. All intercompany transactions and balances have been eliminated in consolidation.

The list of consolidated subsidiaries as of and for the nine months ended September 30, 2004 is as follows:

<u>Name of subsidiary</u>	<u>Location</u>	<u>% of ownership</u>
AnGes, Inc.	U.S.A	100.0%
AnGes Euro Limited	UK	100.0%
GenomIdea Inc.	Japan	61.6%

AnGes has no equity investment which is accounted for under the equity method.

AnGes and its subsidiaries have fiscal year-ends of December 31.

***Cash and Cash equivalents***

For the purpose of consolidated statements of cash flows, “Cash and cash equivalents” consist of cash on hands, demand deposits, and certain investments which are readily convertible to cash, and which mature within three months or less from date of purchase with virtually no risk of loss of values.

“Cash and bank deposits” on the consolidated balance sheets and “Cash and cash equivalents” on the consolidated statements of cash flows are reconciled as follows (in thousands):

	<u>September 30,</u>		<u>December 31,</u>
	<u>2004</u>	<u>2003</u>	<u>2003</u>
Cash and bank deposits.....	¥ 5,639,637	¥ 2,974,334	¥ 6,072,021
Less: Time deposits with original maturities of more than three months.....	(1,500,000)	—	(1,500,000)
Cash and cash equivalents.....	<u>¥ 4,139,637</u>	<u>¥ 2,974,334</u>	<u>¥ 4,572,021</u>

### **Marketable securities and investments in securities**

The Company considers its marketable securities and investments in securities as available-for-sale securities which are not held for trading purposes and not held to maturity with the positive intent and ability to hold maturity. Available-for-sale securities of which the fair market values are readily determinable are recorded at fair market value. Unrealized gains and losses are reported in a separate component of stockholders' equity. Available-for-sale securities of which the fair market values are not readily determinable are recorded at cost. The cost of securities sold is based on the moving average method.

### **Inventories**

Inventories are principally stated at cost. The cost of raw materials is determined using the moving average method, the cost of work in process is determined using the specific identification method, and the cost of supplies is determined using the last purchase price method.

### **Depreciation and Amortization**

#### *Property and equipment*

Depreciation of "Property and equipment" is calculated using the declining-balance method at rates based on the estimated useful lives of the assets which are prescribed by the Japanese Income Tax Laws. Useful lives by asset category are as follows:

Asset category	Years
Buildings and improvements.....	3-15
Machinery.....	3 - 4
Furniture, Laboratory and office equipment.....	3-10

Property and equipment consisted of the following (in thousands):

Asset category	September 30,		December 31,
	2004	2003	2003
Buildings and improvements.....	¥ 204,338	¥ 185,672	¥ 185,659
Machinery.....	86,344	86,344	86,344
Furniture, Laboratory and office equipment.....	270,695	142,955	151,955
	561,378	414,972	423,959
Less: Accumulated depreciation.....	(284,017)	(191,946)	(225,899)
	¥ 277,360	¥ 223,025	¥ 198,059

#### *Intangible assets and goodwill*

Intangible assets and goodwill are carried at cost less accumulated amortization. Capitalized costs for software for internal use are amortized using the straight-line method over 5 years. Goodwill is amortized using the straight-line method over 5 years.

### **Deferred charges**

Stock issuance costs are expensed as incurred.

### **Allowance for doubtful accounts**

“Allowance for doubtful accounts” is maintained for the amounts deemed uncollectible based on solvency analyses and for estimated delinquency based on collection rates projected from historical credit loss experiences, and for the amounts to cover specific accounts that are estimated to be uncollectible.

### **Translation of foreign currency balances and transactions**

Foreign currency transactions are translated using foreign exchange rate prevailing at the transaction dates. Receivables and payables denominated in foreign currencies were translated at the current rate at the balance sheets date. The differences of the prevailing rate between the transaction date and balance sheets date are involved in or charged to income accordingly.

All the assets and liabilities of foreign subsidiaries are translated at current rates at the balance sheets dates. All the income and expense accounts are translated at weighted-average rate. Adjustments arising from translating financial statements of overseas subsidiaries denominated in foreign currencies into Japanese yen are reported in a separate component of stockholders' equity.

### **Lease transactions**

Finance leases, other than those which involve transferring of ownership of the leased assets to the lessee, are accounted for in a manner similar to operating leases.

### **Consumption taxes**

Consumption taxes are excluded from the amounts in the consolidated statements of operations.

## **3. Fair value of financial instruments**

The fair values of available-for-sale securities by type of security and contractual maturity as of September 30, 2004 and December 31, 2003 are as follows (in thousands):

<u>September 30, 2004</u>	<u>Amortized cost</u>	<u>Unrealized gains</u>	<u>Unrealized losses</u>	<u>Estimated fair value</u>
Type of security				
Corporate debt securities.....	¥ 2,600,088	¥ 233	¥ —	¥ 2,600,321
	<u>¥ 2,600,088</u>	<u>¥ 233</u>	<u>¥ —</u>	<u>¥ 2,600,321</u>
<u>December 31, 2003</u>	<u>Amortized cost</u>	<u>Unrealized gains</u>	<u>Unrealized losses</u>	<u>Estimated fair value</u>
Type of security				
Corporate debt securities.....	¥ 2,300,705	¥ —	¥ 1,957	¥ 2,298,748
	<u>¥ 2,300,705</u>	<u>¥ —</u>	<u>¥ 1,957</u>	<u>¥ 2,298,748</u>

As of September 30, 2004 and December 31, 2003, carrying amounts of investments in securities which have no fair market value were ¥1,000 thousand. Investments in securities are classified into "other assets" of consolidated balance sheets.

As of and for the nine months ended September 30, 2003, the Company had no marketable securities and investments in securities.

#### 4. Leases

##### **Finance leases without transfer of ownership as lessee**

Pro forma data as of September 30, 2003 and 2004, and December 31, 2003 as to acquisition cost, accumulated depreciation and net book value of leased assets are summarized as follows (in thousands):

	September 30,		December 31,
	2004	2003	2003
Pro forma acquisition cost.....	¥ 229,128	¥ 223,610	¥ 219,584
Pro forma accumulated depreciation.....	121,623	57,873	60,313
Pro forma net book value.....	¥ 107,505	¥ 165,736	¥ 159,271

Future minimum lease payments under finance leases without transfer of ownership are summarized as follows (in thousands):

	September 30,		December 31,
	2004	2003	2003
Due within one year.....	¥ 57,981	¥ 69,118	¥ 75,058
Thereafter.....	52,529	98,719	86,749
	¥ 110,510	¥ 167,838	¥ 161,807

Lease expenses and pro forma data as to depreciation expenses and interest expenses are summarized as follows (in thousands):

	9 months ended September 30,		Year ended December 31,
	2004	2003	2003
Lease expenses.....	¥ 66,664	¥ 69,622	¥ 90,488
Pro forma depreciation expenses.....	63,919	65,865	86,111
Pro forma interest expenses.....	3,363	4,455	5,796

Depreciation is based on the straight-line method over the lease term of the leased assets with no residual value. The difference between the total lease expenses and the pro forma acquisition cost of leased assets is assumed to be pro forma interest expense and the allocation to each period is based on the interest method.

##### **Operating lease transactions as lessee**

Future minimum lease payments under operating leases are summarized as follows (in thousands):

	September 30,		December 31,
	2004	2003	2003
Due within one year.....	¥ 769	¥ 1,156	¥ 742
Thereafter.....	384	771	928
	¥ 1,154	¥ 1,928	¥ 1,671