

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

TOSHIBA MACHINE CO., LTD. AND CONSOLIDATED SUBSIDIARIES

## 1. Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements of Toshiba Machine Co., Ltd. (the "Company") and consolidated subsidiaries are prepared on the basis of accounting principles generally accepted in Japan, which are different in certain respects as to the application and disclosure requirements of International Financial Reporting Standards, and are compiled from the consolidated financial statements prepared by the Company as required by the securities and Exchange Law of Japan. The preparation of these financial statements 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 these estimates. The consolidated statements of shareholders' equity have been prepared to supply additional information.

The consolidated balance sheets, statements of income and cash flows incorporate certain reclassifications and rearrangements in order to present these statements in forms which are more familiar to readers of these statements outside of Japan. In addition, the notes to the consolidated financial statements include information which is not required under generally accepted accounting principles and practice in Japan but is presented herein as additional information.

## 2. Summary of Significant Accounting Policies

### (a) Basis of consolidation and accounting for investments in unconsolidated subsidiaries and affiliates

The consolidated financial statements include the accounts of the Company and those of its subsidiaries (together the "Companies"). Certain subsidiaries which are not material are not consolidated.

All significant intercompany transactions and accounts and unrealized intercompany profits are eliminated in consolidation.

The difference between the cost and underlying interest in net equity of consolidated subsidiaries at the time of acquisition, which is included in intangible assets of the accompanying consolidated balance sheets, is deferred and amortized within the five-year period.

Investments in affiliates (15 to 50 percent-

owned companies) in which the ability to exercise significant influence exist, except immaterial investments, are stated at cost plus equity in undistributed earnings (losses) of investees.

Net consolidated income (losses) includes the Company's share of the current net earnings (losses) of such companies, after elimination of unrealized intercompany profits.

### (b) Translation of Foreign Currencies

Monetary assets and liabilities denominated in foreign currencies are translated into Japanese yen at the exchange rate prevailing at the balance-sheet date except for those hedged by a forward contract, which are translated using the contracted rate.

The foreign exchange gains and losses from translation are recognized in the consolidated statements of income to the extent that they are not hedged by foreign exchange derivatives.

All assets and liabilities of foreign subsidiaries and affiliates are translated at current rates at the respective balance sheet dates and all income and expense accounts are translated at average rates for the respective periods. The components of shareholders' equity are translated at their historical exchange rates.

### (c) Securities

Securities owned by the companies have been classified into two categories, held-to-maturity securities and other securities, in accordance with accounting standard for financial instruments.

Held-to-maturity securities are carried at amortized cost. Marketable securities classified as other securities are carried at fair value with any changes in unrealized gain or loss, net of income taxes, directly included in shareholders' equity.

Non-marketable securities classified as other securities are carried at cost. Cost of securities sold is determined by the moving average method.

### (d) Inventories

Inventories are stated at the cost, determined by the specific identification method for finished products and work in process, and by the moving average method for raw materials and supplies.

### (e) Allowance for doubtful receivables

The allowance for doubtful receivables is stated based on the default ratio sustained over a specific period in the past and the estimated uncol-

lectible amount based on the analysis of certain individual accounts, including probable bad debts and claims in bankruptcy.

This amount is considered sufficient to cover possible losses on collection.

**(f) Bonuses**

The bonus to the employees are paid twice a year and accrued based on estimated amounts to be paid in the subsequent period. Bonuses to directors and statutory auditors, which are subject to approval by the shareholders, are an appropriation of retained earnings and not charged to income.

**(g) Depreciation of property, plant and equipment**

Depreciation of building is computed, with minor exceptions, by the straightline method and other depreciation of property, plant and equipment is computed by the declining balance method over the estimated useful lives of respective assets.

**(h) Amortization of intangible assets**

Computer software used internally by the Company and consolidated subsidiaries is amortized by the straight-line method over the relevant economic useful lives (5 years). The others are computed by the declining balance method over the estimated useful lives of respective assets.

**(i) Finance Leases**

Finance leases, which do not transfer ownership of the leased assets to the lessees are accounted for in the same manner as operating leases.

**(j) Income Taxes**

The Companies accrue income taxes based on taxable income.

The Companies include many items for financial reporting purpose which, in the case of expenses, are not currently deductible and in the case of income, are not currently taxable.

Income taxes based on temporary differences between tax and financial reporting purposes are reflected as deferred income taxes in the consolidated financial statements using the asset and liability method.

**(k) Employee's Retirement Benefits**

Accrued employees' retirement benefits are provided based on the projected retirement benefit obligation less the fair value of plan assets at year-end.

The unrecognized transitional obligation is being amortized over 15 years. Actuarial gain or loss is amortized by the straight-line method over the average remaining years of service of employees.

**(l) Legal Reserve**

Under the Commercial code of Japan (the "Code") the Company and domestic subsidiaries are required to appropriate as a legal reserve an amount of retained earnings equal to at least 10% of cash dividends and other distributions for each period until such reserve and the amount of capital surplus equals 25% of the common stock. The code also provides that, to the extent that the sum of capital surplus and legal reserve exceeds 25% of the common stock, the amount of any such excess is available for appropriations by resolution of the shareholders.

**(m) Amounts per Share of Common Stock**

Net income (loss) per share is computed based on the weighted-average number of shares of common stock outstanding during each year.

Diluted net income per share is not presented since the Company has never issued any securities with a dilutive effect, such as bonds with warrants and convertible bonds. Cash dividends per share represent the actual amount declared as applicable to the respective years.

**(n) Statements of Cash Flows**

In preparing the statements of cash flows, cash on hand, readily available deposits and short-term highly liquid investments with maturities of not exceeding three months at the time of purchase are considered to be cash and cash equivalents.

**(o) Reclassifications**

Certain accounts in the consolidated financial statements for the year ended March 31, 2004 have been reclassified to conform to the 2005 presentation.

### **3. U.S. Dollar Amounts**

U.S. dollar amounts are included solely for the convenience of the reader and have been translated at the rate of ¥107.39=U.S.\$1, the approximate exchange rate prevailing in the Japanese foreign exchange market on March 31, 2005. This translation should not be construed as a representation that the yen amounts actually represent, have been, or could be converted into U.S. dollars.

#### 4. Securities

Information regarding marketable securities classified as other securities included in investment securities were as follows:

	Millions of yen					
	2005			2004		
	Carrying value	Market value	Unrealized gains	Carrying value	Market value	Unrealized gains
Equity securities	¥1,881	¥6,442	¥4,561	¥1,794	¥5,587	¥3,793
	¥1,881	¥6,442	¥4,561	¥1,794	¥5,587	¥3,793

	Thousands of U.S. dollars		
	2005		
	Carrying value	Market value	Unrealized gains
Equity securities	\$17,516	\$59,987	\$42,471
	\$17,516	\$59,987	\$42,471

#### 5. Property, Plant and Equipment

Property, plant and equipment at March 31, 2005 and 2004 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
	Land	¥6,081	¥6,237
Buildings and structures	30,315	30,362	282,289
Machinery and equipment	31,063	32,247	289,254
Vehicles	575	593	5,354
Tools, furniture and fixtures	7,423	7,384	69,122
Construction in progress	361	112	3,362
	75,818	76,935	706,006
Less accumulated depreciation	(53,610)	(54,739)	(499,208)
	¥22,208	¥22,196	\$206,798

Depreciation expense for the years ended March 31, 2005 and 2004 were ¥ 1,825 million (\$ 16,994 thousand) and ¥ 1,800 million, respectively.

#### 6. Short-term Bank Loans and Long-term Debt

The annual interest rates applicable to the short - term bank loans outstanding on March 31, 2005 and 2004, ranged principally from 0.52% to 4.70%, and from 0.49% to 2.30% respectively. Long-term debt on March 31, 2005 and 2004 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
	Loans, principally from Japanese banks and insurance companies, with pledged assets as collateral, maturing 2006 – 2010 , interest 1.31 % – 2.27 %	¥12,140	12,888
	12,140	12,888	113,046
Less current portion	762	748	7,096
	¥11,378	¥12,140	\$105,950

The aggregate annual maturities of long-term debt at March 31, 2005 were as follows:

Year ending March 31	Millions of yen	Thousands of U.S. dollars
2006	¥762	\$7,096
2007	1,538	14,322
2008	1,140	10,615
2009	8,690	80,920
2010 and later	10	93
	¥12,140	\$113,046

## 7. Employees' Retirement Benefits

The severance indemnity regulation of the Company and certain subsidiaries provides for benefit payments based on the employee's current basic rate of pay and length of service.

The Company and certain subsidiaries have a non-contributory funded pension plan for employees. The Company and certain subsidiaries pay the full cost of the benefits to a bank which act as the trustees.

The liability for employees retirement benefits at March 31, 2005 and 2004 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Projected benefit obligation	¥18,557	¥18,667	\$172,800
Fair value of plan assets	(744)	(1,001)	(6,928)
Unrecognized transitional obligation	(8,011)	(8,930)	(74,597)
Unrecognized actuarial loss	(1,798)	(1,636)	(16,743)
Accrued retirement benefits obligation	¥8,004	¥7,100	\$74,532

The components of net periodic benefit costs for the year ended March 31, 2005 and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Service cost	¥1,007	¥1,187	\$9,377
Interest cost	311	420	2,896
Expected return on plan assets	(7)	(8)	(65)
Recognized actuarial loss	239	326	2,225
Amortization of transitional obligation	827	835	7,701
	¥2,377	¥2,760	\$22,134

Certain consolidated subsidiaries have adopted the conventional method in calculating their projected benefit obligation.

Assumptions used in the accounting for the projected benefit obligation were as follows:

	2005	2004
Discount rate	2.0%	2.0%
Expected rate of return on plan assets	1.0%	1.0%
Amortization period of transitional obligation	15 years	15 years
Amortization period of actuarial loss/gain	10 years	10 years

## 8. Contingent Liabilities

On March 31, 2005 contingent liabilities for notes discounted in the ordinary course of business and for loans guaranteed by the Company, principally on behalf of non-consolidated subsidiaries and affiliated companies, amounted to ¥347 million (\$3,231 thousand) and ¥848 million (\$7,896 thousand), respectively.

## 9. Leases

Finance leases of the Companies other than those where ownership of the leased assets is transferred to the lessee, are accounted for as operating leases. The following pro forma amounts represent the acquisition costs, accumulated depreciation and net book value of the leased assets at March 31, 2005 and 2004, which would have been reflected in the consolidated balance sheet if these arrangements have been accounted for as finance leases:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Acquisition Costs			
Machinery, equipment and vehicles	¥893	¥920	\$8,315
Tools, furniture and fixtures	2,010	2,040	18,717
Less-Accumulated depreciation	(1,386)	(1,566)	(12,906)
Net book value	¥1,517	¥1,394	\$14,126

Future lease payments (including the interest portion thereon) subsequent to March 31, 2005 for finance leases accounted for as operating leases are as follows:

	Millions of yen	Thousands of U.S. dollars
	2005	2005
Due within one year	¥545	\$5,075
Due after one year	972	9,051
	¥1,517	\$14,126

Periodic lease charges, as a lessee, charged to income for the years ended March 31, 2005 and 2004 were ¥ 586 million (\$5,457 thousand) and ¥ 763 million, respectively.

## 10. Pledged Assets

The following assets were pledged as collateral at March 31, 2005:

	Millions of yen	Thousands of U.S. dollars
Property, plant and equipment (Net of accumulated depreciation)	¥5,200	\$48,422

The preceding collaterals were pledged to secure long-term debt amounting to ¥196 million (\$1,825 thousand), short-term bank loans amounting to ¥587 million (\$5,466 thousand).

## 11. Income Taxes

Income taxes in Japan applicable to the Companies generally comprise Corporation Tax, Enterprise Tax and Prefectural and Municipal Inhabitants taxes. The statutory tax rates for the years ended March 31, 2005 and 2004 are approximately 39.8% and 41.1% respectively.

The reconciliation between the statutory rate and effective tax rate of income taxes for the year ended March 31, 2005 and 2004 are as follows:

	2005	2004
Statutory tax rate	<b>39.8 %</b>	41.1 %
Per capita portion of Inhabitant Tax	<b>0.5</b>	0.9
Non-taxable revenue	<b>0.1</b>	0.5
Non-deductible expense	<b>0.5</b>	1.2
Unrealized intercompany profit on fixed asset	<b>(0.0)</b>	(0.1)
Change in valuation allowance	<b>(9.0)</b>	(27.7)
Difference of a tax rate with consolidated subsidiaries	<b>(1.1)</b>	—
Other	<b>(1.9)</b>	0.1
Effective tax rate	<b>28.9 %</b>	16.0 %

The significant components of deferred tax assets and liabilities at March 31, 2005 and 2004 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Deferred tax assets:			
Accrued employees bonuses	<b>¥1,005</b>	¥230	<b>\$9,359</b>
Allowance for doubtful accounts	<b>155</b>	42	<b>1,443</b>
Devaluation of inventories	<b>161</b>	98	<b>1,499</b>
Devaluation of securities	<b>226</b>	4	<b>2,104</b>
Accrued employees' retirement benefits	<b>2,127</b>	69	<b>19,806</b>
Unrealized gain on inventories	<b>117</b>	84	<b>1,090</b>
Other	<b>1,206</b>	355	<b>11,230</b>
Total deferred tax assets	<b>¥4,997</b>	¥882	<b>\$46,531</b>
Valuation allowance	<b>(2,490)</b>	—	<b>(23,186)</b>
Net deferred tax assets	<b>¥2,507</b>	¥882	<b>\$23,345</b>
Deferred tax liabilities:			
Depreciation	<b>(15)</b>	(17)	<b>(140)</b>
Unrealized gain on securities	<b>(1,809)</b>	(1,495)	<b>(16,845)</b>
Deferred tax liabilities	<b>(¥1,824)</b>	(¥1,512)	<b>(\$16,985)</b>
Net deferred tax assets (liabilities)	<b>(¥683)</b>	(¥630)	<b>(\$6,360)</b>

Due to the change in the Corporate Enterprise Tax rate effective for tax period ending March 31, 2005, the Company's statutory tax rate will change from 41.1% to 39.8%.

## 12. Cash and cash equivalents.

Reconciliation between cash and time deposits in the consolidated balance sheets and cash and cash equivalents in the statements of cash flows at March 31, 2005 and 2004 is presented as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Cash and time deposits	<b>¥26,619</b>	¥36,107	<b>\$247,872</b>
Short-term investments	—	¥5	—
Cash and cash equivalents	<b>¥26,619</b>	¥36,112	<b>\$247,872</b>

### 13. Research and development costs

Research and development costs charge to income were ¥2,512 million (\$23,391 thousand) and ¥3,194 million for the years ended March 31, 2005 and 2004 respectively.

### 14. Segment information

#### (a) Business segment information

The Companies' business is classified into the following four segments based on the similarities of type and nature of business:

Molding Machinery: Injection molding machines, Die casting machines, Plastic extrusion

Machine Tools: Large size machine tools, Portal type machine tools, Machining centers, Horizontal boring machines, High-precision machines

Semiconductor Equipment: Electron beam lithography system, Epitaxial reactor system

Other Products: Hydraulic equipment, Electronic controls

The tables below present sales, operating expenses and operating profit information by business segment.

Year ended March 31, 2005	Millions of yen					
	Molding Machinery	Machine Tools	Semiconductor Equipment	Other Products	Eliminations and/or corporate	Consolidated
Sales	¥65,764	¥25,082	¥16,342	¥20,238	¥(3,853)	¥123,573
Operating expenses	60,097	22,089	14,636	18,263	(3,745)	111,340
Operating income	5,667	2,993	1,706	1,975	(108)	12,233
Identifiable assets	56,751	23,480	23,887	31,849	9,090	145,057
Depreciation	927	203	323	372	—	1,825
Capital expenditure	782	268	214	740	—	2,004

Year ended March 31, 2004	Millions of yen					
	Molding Machinery	Machine Tools	Other Products	Eliminations and/or corporate	Consolidated	
Sales	¥60,872	¥18,843	¥34,438	¥(3,495)	¥110,658	
Operating expenses	56,724	18,247	31,462	(3,376)	103,057	
Operating income	4,148	596	2,976	(119)	7,601	
Identifiable assets	57,314	22,474	57,708	10,813	148,309	
Depreciation	1,006	212	582	—	1,800	
Capital expenditure	398	150	1,226	—	1,774	

Effective April 1, 2004 the Company separated their Semiconductor Equipment business which had been included in other products, due to its increased in amount.

Year ended March 31, 2005	Thousands of U.S.dollars					
	Molding Machinery	Machine Tools	Semiconductor Equipment	Other Products	Eliminations and/or corporate	Consolidated
Sales	\$612,385	\$233,560	\$152,174	\$188,453	\$(35,878)	\$1,150,694
Operating expenses	559,615	205,690	136,288	170,062	(34,873)	1,036,782
Operating income	52,770	27,870	15,886	18,391	(1,005)	113,912
Identifiable assets	528,457	218,642	222,432	296,574	84,645	1,350,750
Depreciation	8,632	1,890	3,008	3,464	—	16,994
Capital expenditure	7,282	2,495	1,993	6,891	—	18,661

(b) Geographic segment information of the Companies for the year ended March 31, 2005 and 2004 were as follows:

Year ended March 31, 2005	Millions of yen					
	Japan	North America	Asia	Total	Eliminations	Consolidated
Net sales	¥121,009	¥7,829	¥7,453	¥136,291	¥(12,718)	¥123,573
Cost and expenses	109,297	7,707	6,985	123,989	(12,649)	111,340
Operating income	11,712	122	468	12,302	(69)	12,233
Identifiable assets	125,517	4,846	6,038	136,401	8,656	145,057

Year ended March 31, 2004	Millions of yen					
	Japan	North America	Asia	Total	Eliminations	Consolidated
Net sales	¥106,345	¥10,941	¥3,083	¥120,369	¥(9,711)	¥110,658
Cost and expenses	99,127	10,838	3,019	112,984	(9,927)	103,057
Operating income	7,218	103	64	7,385	216	7,601
Identifiable assets	125,719	7,491	2,065	135,275	13,034	148,309

Year ended March 31, 2005	Thousands of U.S.dollars					
	Japan	North America	Asia	Total	Eliminations	Consolidated
Net sales	\$1,126,818	\$72,903	\$69,401	\$1,269,122	\$(118,428)	\$1,150,694
Cost and expenses	1,017,758	71,767	65,043	1,154,568	(117,786)	1,036,782
Operating income	109,060	1,136	4,358	114,554	(642)	113,912
Identifiable assets	1,168,796	45,125	56,225	1,270,146	80,604	1,350,750

(c) Sales to foreign customers for the years ended March 31, 2005 and 2004 were as follows:

Year ended March 31, 2005	Millions of yen			
	North America	Asia	Other	Total
Sales to foreign customers	¥14,774	¥40,354	¥4,452	¥59,580
Net sales	—	—	—	123,573
Ratio of Sales to foreign Customers (%)	12.0	32.7	3.5	48.2

Year ended March 31, 2004	Millions of yen			
	North America	Asia	Other	Total
Sales to foreign customers	¥19,073	¥32,243	¥5,856	¥57,172
Net sales	—	—	—	110,658
Ratio of Sales to foreign Customers (%)	17.2	29.1	5.4	51.7

Year ended March 31, 2005	Thousands of U.S.dollars			
	North America	Asia	Other	Total
Sales to foreign customers	\$137,573	\$375,771	\$41,456	\$554,800
Net sales	—	—	—	1,150,694
Ratio of Sales to foreign Customers (%)	12.0	32.7	3.5	48.2

## 15. Other

A consolidated subsidiary, Toshiba Machine Company, America ("TMA") which is a defendant in a legal lawsuit, was ordered by a lower court in March 2003 to pay to the plaintiff a sum of \$9.3 million to compensate for alleged losses incurred regarding one of our machine tools. Although TMA contested this decision, their appeal was overruled and was ordered by the court of appeals to pay \$9.3 million with 10% interest calculated from the day of the lower court ruling to the date of payment. Based on the advice of their attorneys, TMA has petitioned for a rehearing of their appeal and is currently under litigation. Based on the opinion of their lawyers, TMA has withheld paying \$2.2 million.