

**CHUGOKU MARINE PAINTS, LTD.**

**Consolidated Financial Statements**

**for the years ended 31 March 2007, 2008 and 2009**



## Report of Independent Auditors

The Board of Directors  
CHUGOKU MARINE PAINTS, LTD.

We have audited the accompanying consolidated balance sheets of CHUGOKU MARINE PAINTS, LTD. and consolidated subsidiaries as of 31 March 2008 and 2009 and the related consolidated statements of income, changes in net assets, and cash flows for each of the three years in the period ended 31 March, 2009, all expressed in yen. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of CHUGOKU MARINE PAINTS, LTD. and consolidated subsidiaries as of 31 March, 2008 and 2009, and the consolidated results of their operations and their cash flows for each of the three years in the period ended 31 March, 2009 in conformity with accounting principles generally accepted in Japan.

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended 31 March 2009 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 3 to the consolidated financial statements.

25 June , 2009

*Ernst & Young ShinNihon LLC*

*Ernst & Young ShinNihon LLC*

# CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

## Consolidated Balance Sheets 31 March 2008 and 2009

ASSETS	Millions of Yen		Thousands of U.S. Dollars (Note 3)
	<u>2008</u>	<u>2009</u>	<u>2009</u>
Current Assets:			
Cash on hand and in banks (Note 14)	¥ 7,976	¥ 8,625	\$ 87,806
Trade notes and accounts receivable	36,538	34,892	355,206
Less, allowance for doubtful accounts	(701)	(646)	(6,575)
	<u>35,837</u>	<u>34,246</u>	<u>348,631</u>
Inventories (Note 4)	17,719	16,004	162,920
Deferred tax assets (Note 15)	736	841	8,565
Other current assets	<u>1,299</u>	<u>913</u>	<u>9,294</u>
Total current assets	<u>63,567</u>	<u>60,629</u>	<u>617,216</u>
Property, plant and equipment:			
Buildings and structures	15,844	13,842	140,911
Machinery, equipment and vehicles	12,527	11,128	113,285
Tools, furniture and fixtures	<u>3,305</u>	<u>3,255</u>	<u>33,141</u>
	<u>31,676</u>	<u>28,225</u>	<u>287,337</u>
Less, accumulated depreciation	(20,922)	(18,498)	(188,313)
	<u>10,754</u>	<u>9,727</u>	<u>99,024</u>
Land (Note 12)	14,538	13,125	133,611
Construction in progress	<u>279</u>	<u>986</u>	<u>10,037</u>
Total property, plant and equipment	<u>25,571</u>	<u>23,838</u>	<u>242,672</u>
Investments and other assets:			
Investments in securities (Note 5)	7,291	4,959	50,484
Deferred tax assets (Note 15)	370	381	3,874
Other assets	<u>1,752</u>	<u>1,969</u>	<u>20,052</u>
Total investments and other assets	<u>9,413</u>	<u>7,309</u>	<u>74,410</u>
Total assets	<u>¥ 98,551</u>	<u>¥ 91,776</u>	<u>\$ 934,298</u>

The accompanying notes are an integral part of these consolidated financial statements.

# CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

## Consolidated Balance Sheets 31 March 2008 and 2009

LIABILITIES AND NET ASSETS	Millions of Yen		Thousands of U.S. Dollars (Note 3)
	<u>2008</u>	<u>2009</u>	<u>2009</u>
Current liabilities:			
Short-term loans (Note 7)	¥ 25,886	¥ 24,940	\$ 253,893
Current portion of long-term debt (Note 7)	630	150	1,525
Notes and accounts payable:			
Trade	15,866	13,193	134,312
Other	3,288	2,749	27,983
	<u>19,154</u>	<u>15,942</u>	<u>162,295</u>
Income taxes payable (Note 15)	1,480	786	7,999
Deferred tax liabilities (Note 15)	4	–	–
Other current liabilities	<u>2,568</u>	<u>2,534</u>	<u>25,798</u>
Total current liabilities	<u>49,722</u>	<u>44,352</u>	<u>451,510</u>
Non-current liabilities:			
Long-term debt (Note 7)	2,555	3,002	30,560
Accrued severance indemnities (Note 8)	692	660	6,719
Deferred tax liabilities on land revaluation (Notes 12 and 15)	3,044	3,027	30,813
Deferred tax liabilities (Note 15)	794	33	337
Other liabilities	639	688	7,013
Total non-current liabilities	<u>7,724</u>	<u>7,410</u>	<u>75,442</u>
Total liabilities	<u>57,446</u>	<u>51,762</u>	<u>526,952</u>
Commitments and contingent liabilities (Note 9)			
Net assets:			
Shareholders' equity			
Common stock,			
Authorized: 277,630,000 shares;	11,626	11,626	118,356
Issued 69,068,822 shares at 31 March 2008 and 2009			
Capital surplus	7,786	7,784	79,240
Retained earnings	17,764	21,211	215,932
Common stock in treasury, at cost:			
31 March 2008-252,059 shares	(156)		
31 March 2009-309,704 shares		(188)	(1,910)
Total shareholders' equity	<u>37,020</u>	<u>40,433</u>	<u>411,618</u>
Valuation, translation adjustments and other			
Revaluation gain on land (Note 12)	2,526	3,169	32,259
Net unrealized holding gain (loss) on other securities	1,498	(15)	(155)
Foreign currency translation adjustments	(2,225)	(5,735)	(58,384)
Total valuation, translation adjustments and other	<u>1,799</u>	<u>(2,581)</u>	<u>(26,280)</u>
Minority interests	<u>2,286</u>	<u>2,162</u>	<u>22,008</u>
Total net assets	<u>41,105</u>	<u>40,014</u>	<u>407,346</u>
Total liabilities and net assets	<u>¥ 98,551</u>	<u>¥ 91,776</u>	<u>\$ 934,298</u>

The accompanying notes are an integral part of these consolidated financial statements.

## CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

### Consolidated Statements of Income For the years ended 31 March 2007, 2008 and 2009

	Millions of Yen			Thousands of U.S. Dollars (Note 3)
	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2009</u>
Net sales	¥ 88,197	¥ 104,799	¥ 103,623	\$ 1,054,899
Cost of sales	<u>62,542</u>	<u>76,062</u>	<u>74,551</u>	<u>758,940</u>
Gross profit	25,655	28,737	29,072	295,959
Selling, general and administrative expenses (Note 13)	<u>18,397</u>	<u>20,605</u>	<u>20,642</u>	<u>210,144</u>
Operating income	<u>7,258</u>	<u>8,132</u>	<u>8,430</u>	<u>85,815</u>
Other income (expenses):				
Interest and dividend income	263	272	254	2,587
Interest expense	(742)	(1,159)	(775)	(7,885)
Gain on sales of investments in securities, net	–	174	0	1
Gain (loss) on sales of property, plant and equipment, net	6	(11)	12	125
Loss on impairment of fixed assets	(11)	–	–	–
Foreign currency exchange gain (loss)–net	81	(162)	(431)	(4,392)
Royalty income	72	110	116	1,182
Revenue from technical training	125	157	124	1,267
Net provision for product warranties	–	39	8	82
Compensation for relocation	–	424	–	–
Other–net	<u>63</u>	<u>60</u>	<u>9</u>	<u>81</u>
Other income–net	<u>(143)</u>	<u>(96)</u>	<u>(683)</u>	<u>(6,952)</u>
Income before income taxes and minority interests	<u>7,115</u>	<u>8,036</u>	<u>7,747</u>	<u>78,863</u>
Income taxes (Note 15):				
Current	1,760	2,141	2,116	21,542
Deferred	<u>75</u>	<u>190</u>	<u>(119)</u>	<u>(1,211)</u>
	1,835	2,331	1,997	20,331
Minority interests in earnings of consolidated subsidiaries	<u>(427)</u>	<u>(587)</u>	<u>(718)</u>	<u>(7,309)</u>
Net income	<u>¥ 4,853</u>	<u>¥ 5,118</u>	<u>¥ 5,032</u>	<u>\$ 51,223</u>
		Yen		U.S. Dollars
Earnings per share:				
Net income	¥ 70.47	¥ 74.35	¥ 73.14	\$ 0.74
Cash dividends applicable to the year	10.00	13.00	13.00	0.13
Weighted average number of shares (in thousands)	68,870	68,832	68,790	

The accompanying notes are an integral part of these consolidated financial statements.



# CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

## Consolidated Statements of Changes in Net Assets For the years ended 31 March 2007, 2008 and 2009

	Thousands of U.S. Dollars (Note 3)					
	Shareholders' equity					
	Number of shares of common stock issued (Thousands)	Common stock	Capital surplus	Retained earnings	Common stock in treasury, at cost	Total shareholders' equity
Balance at 31 March 2008	69,069	\$ 118,356	\$ 79,260	\$ 180,846	\$ (1,590)	\$ 376,872
Net income				51,223		51,223
Cash dividends				(9,107)		(9,107)
Acquisition of treasury stock					(423)	(423)
Disposal of treasury stock			(20)		103	83
Reversal of revaluation gain on land				(7,030)		(7,030)
Net changes in items other than shareholders' equity						
Total changes in items during the year		—	(20)	35,086	(320)	34,746
Balance at 31 March 2009	69,069	\$ 118,356	\$ 79,240	\$ 215,932	\$ (1,910)	\$ 411,618
	Valuation, translation adjustments and other					
	Revaluation gain on land	Net unrealized holding gain on other securities	Foreign currency translation adjustments	Total valuation, translation adjustment and other	Minority Interest	Total net assets
Balance at 31 March 2008	\$ 25,715	\$ 15,246	\$ (22,650)	\$ 18,311	\$ 23,275	\$ 418,459
Net income						51,223
Cash dividends						(9,107)
Acquisition of treasury stock						(424)
Disposal of treasury stock						83
Reversal of revaluation gain on land						(7,030)
Net changes in items other than shareholders' equity	6,544	(15,401)	(35,734)	(44,591)	(1,267)	(45,858)
Total changes in items during the year	6,544	(15,401)	(35,734)	(44,591)	(1,267)	(11,113)
Balance at 31 March 2009	\$ 32,259	\$ (155)	\$ (58,384)	\$ (26,280)	\$ 22,008	\$ 407,346

The accompanying notes are an integral part of these consolidated financial statements.

# CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows For the years ended 31 March 2007, 2008 and 2009

	Millions of Yen			Thousands of U.S. Dollars (Note 3)
	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2009</u>
Cash flows from operating activities:				
Income before income taxes and minority interests	¥ 7,115	¥ 8,036	¥ 7,747	\$ 78,863
Depreciation and amortization	1,229	1,458	1,556	15,835
Loss on impairment of fixed assets	11	–	–	–
Increase in allowance for doubtful accounts	65	111	49	498
Increase (decrease) in accrued severance indemnities	27	(34)	12	125
Decrease in allowance for retirement benefits to directors and corporate auditors	(899)	–	–	–
Interest and dividend income	(263)	(272)	(254)	(2,587)
Interest expense	742	1,159	775	7,885
Foreign currency exchange loss (gain), net	3	13	(10)	(99)
Gain on sales of investments in securities, net	–	(174)	(0)	(1)
Write-down of golf club membership	–	6	14	144
Loss on sales of property, plant and equipment, net	78	34	23	230
Increase in trade notes and accounts receivable	(10,320)	(4,600)	(3,083)	(31,381)
Increase in inventories	(4,575)	(976)	(310)	(3,161)
Increase in trade notes and accounts payable	4,873	297	111	1,131
(Decrease) increase in outstanding discounted notes	(442)	776	193	1,965
Other—net	495	653	433	4,416
Subtotal	(1,861)	6,487	7,256	73,863
Interest and dividend income received	246	330	254	2,590
Interest expense paid	(744)	(1,153)	(783)	(7,972)
Receipt of compensation for relocation	–	911	–	–
Income taxes paid	(1,343)	(1,728)	(2,653)	(27,007)
Net cash (used in) provided by operating activities	(3,702)	4,847	4,074	41,474
Cash flows from investing activities:				
Increase in time deposits	(328)	–	(32)	(321)
Decrease in time deposits	–	228	102	1,042
Payments for purchases of investments in securities	(98)	(307)	(19)	(194)
Proceeds from sales of investments in securities	–	206	3	33
Payments for purchases of property, plant and equipment	(2,631)	(2,572)	(3,009)	(30,635)
Proceeds from sales of property, plant and equipment	46	53	1,647	16,771
Other—net	56	(229)	(326)	(3,333)
Net cash used in investing activities	¥ (2,955)	¥ (2,621)	¥ (1,634)	\$ (16,637)

The accompanying notes are an integral part of these consolidated financial statements.

## CHUGOKU MARINE PAINTS, LTD. AND SUBSIDIARIES

### Consolidated Statements of Cash Flows For the years ended 31 March 2007, 2008 and 2009

	Millions of Yen			Thousands of U.S. Dollars (Note 3)
	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2009</u>
Cash flows from financing activities:				
Increase in short-term loans, net	¥ 5,101	¥ 42	¥ 423	\$ 4,311
Increase in long-term debt	500	–	100	1,018
Repayment of long-term debt	(630)	(130)	(133)	(1,357)
Payments for purchases of treasury stock	(21)	(55)	(42)	(424)
Proceeds from sales of treasury stock	1	1	8	83
Cash dividends	(517)	(1,100)	(893)	(9,095)
Other–net	(65)	(177)	(174)	(1,777)
Net cash provided by (used in) financing activities	<u>4,369</u>	<u>(1,419)</u>	<u>(711)</u>	<u>(7,241)</u>
Effect of exchange rate changes on cash and cash equivalents	394	(711)	(995)	(10,128)
Net (decrease) increase in cash and cash equivalents	(1,894)	96	734	7,468
Cash and cash equivalents at beginning of year	9,647	7,753	7,858	80,000
Increase of cash and cash equivalents resulting from a merger	–	10	–	–
Cash and cash equivalents at end of year (Note 14)	<u>¥ 7,753</u>	<u>¥ 7,858</u>	<u>¥ 8,592</u>	<u>\$ 87,468</u>

The accompanying notes are an integral part of these consolidated financial statements.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 1. Basis of presentation of consolidated financial statements

The accompanying consolidated financial statements of CHUGOKU MARINE PAINTS, LTD. (the “Company”) and consolidated subsidiaries (collectively, the “Companies”) have been 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 have been compiled from the consolidated financial statements prepared by the Company as required by the Japanese Financial Instruments and Exchange rule.

Japanese accounting standards does not require retroactive adjustments on the financial statements but require to disclose the amounts of impact on net income where the Company adopted the new accounting standards. Such impacts are disclosed on the respective footnotes.

As permitted under the Financial Instruments and Exchange Law, amounts of less than one million yen have been omitted. As a result, the totals shown in the accompanying consolidated financial statements (both in yen and in U.S. dollars) do not necessarily agree with the sums of the individual amounts.

Certain amounts from prior years have been reclassified to conform to the current year’s presentation.

In preparing the accompanying consolidated financial statements, certain reclassifications and rearrangements have been made to the Company’s consolidated financial statements issued domestically in order to present them in a format which is more familiar to readers outside Japan.

### 2. Summary of significant accounting policies

#### (1) Principles of consolidation

The accompanying consolidated financial statements include the accounts of the Companies. As at 31 March 2008 and 2009, the Company consolidated 27 and 25 subsidiaries, respectively. All significant inter-company accounts and transactions have been eliminated in consolidation.

The Company revalues assets and liabilities of consolidated subsidiaries at fair market value at the respective dates of acquisition of control.

Any difference between the cost of an investment in a subsidiary and the amount of underlying equity in net assets (goodwill or negative goodwill) is treated as an asset or a liability, and amortized on a straight-line basis over a period of five years.

The fiscal year-ends of consolidated subsidiaries are December 31, except for Kobe Paints, Ltd., which has its year-end at 31 March. For consolidation purposes, the Company uses financial statements with a year end of 31 December of these subsidiaries except for Kobe Paints, Ltd. with necessary consolidation adjustments made to reflect any significant transactions which occurred between 1 January and 31 March.

As at 31 March 2008 and 2009, there were no unconsolidated subsidiaries or affiliates accounted for by the equity method.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

(2) Cash and cash equivalents

Cash and cash equivalents in the consolidated statements of cash flows are composed of cash on hand, bank deposits withdrawable on demand, and short-term investments with an original maturity of three months or less and which are readily convertible to cash and represent a minor risk of fluctuation in value.

(3) Translation of foreign currencies

The Company translates the revenue and expense accounts of the overseas consolidated subsidiaries at the average rates of exchange in effect during the year. The balance sheet accounts, except for the components of shareholders' equity, are translated into yen at the rates of exchange in effect at the balance sheet date. The components of shareholders' equity are translated at their historical exchange rates. Differences arising from translation where two exchange rates have been used are presented under "Foreign currency translation adjustments" and "Minority interests" which are components of net assets.

Current and non-current monetary assets and liabilities denominated in foreign currencies of the Company and its domestic consolidated subsidiaries are translated into yen at the exchange rates in effect at the balance sheet date, except for those hedged by forward foreign exchange contracts which are translated at the contracted rates. All revenues and expenses are translated at the average rates of exchange during the year. Gains and losses arising from foreign exchange translation differences are credited or charged to income in the year in which they are made or incurred, except for those arising from forward foreign exchange contracts.

(4) Changes to other important matters for preparation of the consolidated financial statement

Accounting methods applicable to overseas subsidiaries and used for the consolidated financial statement:

Effective the year ended 31 March 2009, the Company adopted the "Practical Solution on Unification of Accounting Policies Applied to Foreign Subsidiaries for Consolidated Financial Statements" (PITF No.18, issued on 17 May 2006). This change has little impact on operating income and income before income taxes and minority interests for the year ended 31 March 2009.

(5) Investments in securities

Held-to-maturity bonds are either amortized or accumulated to face value. Other securities with quoted market prices are carried at market value. The difference between the acquisition cost and the carrying value of other securities, including unrealized gain and loss, net of the applicable income taxes, is recognized as a component of net assets and is reflected as "Net unrealized holding gain (loss) on other securities." The cost of other securities sold is computed by the moving average method. Other securities without quoted market prices are stated at cost based on the moving-average method.

If a decline in fair value below cost of an individual security is deemed to be material and other than temporary, the carrying value of the individual security is written down.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### (6) Derivatives and hedge accounting

All derivatives are stated at fair value, with changes in fair value included in net income or loss for the period in which they arise unless derivative instruments are used for hedging purposes. Certain overseas subsidiaries utilize forward foreign exchange contracts to reduce the risk arising from exchange rate fluctuations in foreign-currency-denominated receivables and payables. They translate the receivables and payables hedged by forward foreign exchange contracts at the corresponding forward foreign exchange contract rates if the contracts meet certain conditions.

At inception, date of the forward foreign exchange contracts are fixed at the same amount and at the same maturing as the hedged items in accordance with the Company's risk management objective and policy for undertaking the hedge. As certain overseas subsidiaries deem the hedging relationship regarding exchange rate fluctuations to be highly effective, the evaluation of hedge effectiveness at the fiscal year-end is not performed.

### (7) Allowance for doubtful accounts

Allowance for doubtful accounts is provided to cover possible losses on uncollectible accounts. It consists of an estimated uncollectible amount with respect to identified doubtful receivables and an amount calculated based on the historical bad debt ratio with respect to the remaining receivables.

### (8) Inventories

Inventories are mainly stated at cost determined by the moving-average method. Balance sheet amounts are calculated based on the method of reducing the book value in accordance with any decline in profitability.

Previously, inventories were mainly stated at cost, cost being determined by the moving-average method.

The Company adopted "Accounting Standard for Measurement of Inventories" (ASBJ Statement No. 9, issued on 5 July 2006) effective the year ended 31 March 2009. The change of this accounting policy resulted in decrease of operating income and income before income taxes and minority interests in the amount of ¥33 million (\$340 thousand), respectively for the year ended 31 March 2009, compared with the amounts under the previous method.

### (9) Property, plant and equipment and depreciation (except leased assets)

Property, plant and equipment are stated on the basis of cost. The Company calculates depreciation principally by the declining-balance method based on the estimated useful lives of the respective assets, except for buildings (exclusive of any structures attached to the buildings) acquired on or after 1 April 1998 which are depreciated by the straight-line method.

The range of estimated useful lives is summarised as follows:

Buildings and structures	7 - 50 years
Machinery, equipment and vehicles	4 - 17 years
Tools, furniture and fixtures	2 - 10 years

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

Effective the year ended 31 March 2008, pursuant to an amendment to the Corporation Tax Law, the Company and its domestic consolidated subsidiaries have adopted the depreciation method stipulated by the amended Corporation Tax Law for the property, plant and equipment acquired on or after 1 April 2007. As a result, operating income and income before income taxes and minority interests decreased by ¥27 million, respectively, compared with the amounts under the previous method. In addition, the residual values (5% of the acquisition cost) of the property, plant and equipment acquired on or before 31 March 2007 which were fully depreciated based on the Corporation Tax Law before the amendment are depreciated equally over five years starting from the year ended 31 March 2008. As a result, for the year ended 31 March 2008, operating income and income before income taxes and minority interests decreased by ¥60 million, respectively, compared with the amounts under the previous method.

Effective the year ended 31 March 2009, pursuant to an amendment to the Corporation Tax Law, the Company and its domestic consolidated subsidiaries have reviewed the useful lives of machinery and equipment and their classification of assets. As a result, operating income and income before taxes and minority interests decreased by ¥19 million (\$197 thousand), respectively for the year ended 31 March 2009, compared with the amounts under the previous method.

### (10) Loss on impairment of fixed assets

In accordance with the accounting standard for impairment of fixed assets, the Company and its domestic consolidated subsidiaries periodically review their fixed assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company and its domestic consolidated subsidiaries recognize an impairment loss in their statement of income if certain indicators of asset impairment exist and if the book value of an asset exceeds the undiscounted sum of its future cash flows. The standard states that impairment losses should be measured as the excess of the book value over the higher of (1) the fair market value of the asset, net of disposition costs, or (2) the present value of future cash flows arising from ongoing utilization of the asset and from its disposal after use. The standard covers land, factories, buildings and other forms of property, plant and equipment as well as intangible assets. Fixed assets are to be grouped at the lowest levels for which there are identifiable cash flows which are independent of the cash flows from other groups of assets.

### (11) Intangible assets (except leased assets)

Intangible assets, included in other assets, are amortized on a straight-line basis over the period stipulated in the Corporation Tax Law of Japan, except for computer software for internal use which is amortized on a straight-line basis over its estimated useful lives (three to five years).

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### (12) Leases

The capitalized leased assets are depreciated on a straight-line basis over the respective lease terms with a zero residual value.

On 30 March 2007, the Accounting Standards Board of Japan (“ASBJ”) revised ASBJ Statement No. 13, “Accounting Standard for Lease Transactions” and ASBJ Guidance No. 16, “Guidance on Accounting Standard for Lease Transactions,” which revised the accounting standard for lease transactions issued on 17 June 1993. The revised accounting standard for lease transactions, which requires that all finance lease transactions be capitalized, is effective for fiscal years beginning on or after 1 April 2008.

Effective 1 April 2008, the Company adopted this revised standard for lease transactions entered into on and after that date and depreciates capitalized leased assets on the straight-line method over the respective lease terms with a zero residual value.

For finance lease transactions entered into before 1 April 2008, all leased assets were capitalized at the outstanding future lease payments as of 31 March 2008 as the acquisition cost. The imputed interest expenses portion was included in the acquisition cost because the balance of the outstanding future lease payments was immaterial as of 31 March 2008.

The total balance of capitalized leased assets, in the amount of ¥131 million (\$1,340 thousand), was included in machinery, equipment and vehicles as of 31 March 2009. Associated lease obligations were included in other current liabilities and other liabilities, amounting to ¥46 million (\$473 thousand) and ¥91 million (\$927 thousand), respectively as of 31 March 2009. The adoption of this revised standard has no effect on operating income and income before taxes and minority interests for the year ended 31 March 2009.

In the fiscal year ended 31 March 2007 and 2008, all finance lease contracts other than those in which the ownership of the leased asset is to be transferred to leases are accounted for in a method similar to operating lease contracts.

### (13) Accrued bonuses

Accrued bonuses are included in other current liabilities. Certain subsidiaries provide for accrued bonuses for employees based on the amount estimated to be paid.

### (14) Accrued severance indemnities

The Companies, excluding certain overseas subsidiaries, provide for accrued severance indemnities in preparation for payments of retirement benefits to employees at an amount based on the projected benefit obligation attributed to services rendered during the year reduced by pension plan assets at fair value at the end of the year.

The net retirement benefit obligation at transition of ¥1,296 million at the date of adoption is amortized by the straight-line method over a period of 15 years. Actuarial gain or loss is amortized by the straight-line method over a period of 10 years from the year following the year in which it arises.

Accrued severance indemnities in the accompanying consolidated balance sheets included retirement benefits to advisors, counselors and directors amounting to ¥40 million and ¥20 million (\$208 thousand) at 31 March 2008 and 2009, respectively.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

(15) Retirement benefits to directors and corporate auditors

The Company had provided a reserve for directors' and corporate auditors' retirement benefits at 100% of the estimated amounts payable at the end of the fiscal year in accordance with the Company's bylaws. However, the Company abolished the retirement benefits to the directors and corporate auditors pursuant to resolutions approved at a meeting of the board of directors and corporate auditors held on 25 April 2006 and at an annual general shareholders' meeting held on 29 June 2006, for the discontinuance of payments of the retirement benefits to the directors and corporate auditors. Consequently, accrued retirement benefits to the directors and corporate auditors were fully reversed and the amount corresponding to the accrued retirement benefits recorded for the period by 29 June 2006 were included in "Other current liabilities" and "Other liabilities" in the accompanying consolidated balance sheets at 31 March 2008 and 2009.

(16) Product warranty costs

Product warranty costs are included in "Other current liabilities." Provision for estimated warranty costs is recorded based on the ratio of actual warranty costs incurred for the year against the related annual sales amount.

(17) Income taxes

Income taxes of the Company and its domestic subsidiaries consist of corporate income tax, local inhabitant taxes and enterprise tax.

Deferred income taxes are determined using the asset and liability method, whereby deferred tax assets and liabilities are recognized in respect of temporary differences between the tax bases of the assets and liabilities and the amounts reported in the financial statements.

(18) Consumption taxes

The consumption taxes paid and withheld on purchases and sales of goods and services are not included in the respective amounts of cost, expense or revenue in the accompanying consolidated statements of income. The net balance of consumption taxes withheld and paid is included in "Other current assets" or "Other current liabilities" in the accompanying consolidated balance sheets.

(19) Earnings and cash dividends per share

Basic earnings per share of common stock are based on the weighted average number of shares of common stock outstanding during each period.

Diluted earnings per share for the years ended March 31 2007, 2008 and 2009 have not been presented, as the Company had no potentially dilutive shares of common stock.

Cash dividends per share presented in the accompanying consolidated statements of income are applicable to the respective years and include dividends to be paid subsequent to the end of the year. Dividends are charged to retained earnings in the year in which they are paid.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### (20) Shareholders' equity

The Corporation Law of Japan (the "Law") provides that an amount equal to 10% of the amount to be disbursed as distributions of capital surplus (other than the capital reserve) and retained earnings (other than the legal reserve) be transferred to the capital reserve and the legal reserve, respectively, until the sum of the capital reserve and the legal reserve equals 25% of the capital stock account. Such distributions can be made at any time by resolution of the shareholders, or by the board of directors if certain conditions are met.

### 3. United States dollar amounts

Amounts in U.S. dollars are included solely for the convenience of readers outside Japan. The rate of ¥98.23 = U.S. \$1.00, the rate of exchange prevailing at 31 March 2009, has been used in translation. The inclusion of such amounts is not intended to imply that Japanese yen has been or could be readily converted, realized or settled in U.S. dollars at this or any other rate.

### 4. Inventories

Inventories at 31 March 2008 and 2009 comprised of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2008	2009	2009
Merchandise and finished goods	¥ 10,919	¥ 9,526	\$ 96,973
Raw materials and supplies	6,168	5,973	60,805
Work in process	633	505	5,142
Total	¥ 17,719	¥ 16,004	\$ 162,920

Loss on valuation of inventories of ¥169 million (\$1,717 thousand) after recognizing write downs due to decline in profitability was included in cost of sales for the year ended 31 March 2009.

**CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES**

**Notes to Consolidated Financial Statements**

**31 March 2007, 2008, 2009**

**5. Investments in securities**

Other securities and held-to-maturity bonds at 31 March 2008 are summarized as follows:

	Millions of Yen			
	Acquisition cost	Fair value	Gross unrealized gain	Gross unrealized loss
Other Securities:				
Market value available	¥ 3,787	¥ 6,119	¥ 2,415	¥ (83)
Market value not available	1,172	1,172	-	-
Total other securities	¥ 4,959	¥ 7,291	¥ 2,415	¥ (83)
Held-to-maturity bonds:				
Market value available	¥ 3	¥ 3	¥ 0	¥ -
Market value not available	-	-	-	-
Total held-to-maturity bonds	¥ 3	¥ 3	¥ 0	¥ -

The redemption schedule for other securities with maturity dates and held-to-maturity bonds at 31 March 2008 is as follows:

	Millions of Yen	
	Other securities	Held-to-maturity bonds
Due within 1 year	¥ -	¥ 3
	¥ -	¥ 3

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

Other securities at 31 March 2009 are summarized as follows:

	Millions of Yen			
	Acquisition cost	Fair value	Gross unrealized gain	Gross unrealized loss
Other Securities:				
Market value available	¥ 3,798	¥ 3,787	¥ 526	¥ (537)
Market value not available	1,172	1,172	–	–
Total other securities	<u>¥ 4,970</u>	<u>¥ 4,959</u>	<u>¥ 526</u>	<u>¥ (537)</u>

	Thousands of U.S. Dollars			
	Acquisition cost	Fair value	Gross unrealized gain	Gross unrealized loss
Other Securities:				
Market value available	\$ 38,668	\$ 38,552	\$ 5,351	\$ (5,467)
Market value not available	11,932	11,932	–	–
Total other securities	<u>\$ 50,600</u>	<u>\$ 50,484</u>	<u>\$ 5,351</u>	<u>\$ (5,467)</u>

Impairment loss for the years ended 31 March 2008 and 2009 amounted to ¥ 13 million and ¥7 million (\$75 thousand), respectively. Total sales of other securities for the years ended 31 March 2008 and 2009 amounted to ¥206 million and ¥3 million (\$33 thousand), respectively and the related net gain amounted to ¥174 million and ¥0 million (\$1 thousand), respectively.

## 6. Leases

### Finance leases

Information on finance leases other than those which are deemed to transfer the ownership of the leased assets to lessees and other relevant information for the fiscal year ended 31 March 2008 are summarized below.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

- a) *Pro forma* information relating to acquisition cost, accumulated depreciation and net book value on an “as if capitalized” basis at 31 March 2008 is as follows:

	Millions of Yen		
	2008		
	Machinery, equipment and vehicles	Tools, furniture and fixtures	Total
Acquisition cost	¥ 29	¥ —	¥ 29
Accumulated depreciation	12	—	12
Net book value	¥ 17	¥ —	¥ 17

The *pro forma* acquisition cost information is calculated at an amount including the imputed interest expense portion as the balance of outstanding future lease payments was immaterial to the year-end balance of property, plant and equipment.

- b) *Pro forma* information relating to outstanding future lease payments on an “as if capitalised” basis subsequent to 31 March 2008 is as follows:

	Millions of Yen	
	2008	
Due within one year	¥	6
Due after one year		11
Total	¥	17

The *pro forma* information for the outstanding future lease payments is calculated at an amount including the imputed interest expense portion, as the balance of outstanding future lease payments was immaterial to the year-end balance of property, plant and equipment.

- c) Total lease payments for the years ended 31 March 2008 was ¥4 million. Depreciation expense which has not been reflected in the accompanying consolidated statements of income, computed by the straight-line method over the respective lease terms with a zero residual value, would have been the same as the lease payments for the years ended 31 March 2008.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### Operating leases

The amounts of outstanding future lease payments for operating lease transactions subsequent to 31 March 2008 and 2009 were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2008	2009	2009
Due within one year	¥ 93	¥ 316	\$ 3,213
Due after one year	250	145	1,477
Total	¥ 343	¥ 461	\$ 4,690

### 7. Short-term loans and long-term debt

Short-term loans from banks outstanding consisted primarily of six-month notes issued by the Company to banks bearing interest at the weighted average interest rate of 3.4% and 1.7% at 31 March 2008 and 2009, respectively. Customarily, these notes are renewed at maturity subject to re-negotiation of the interest rates and other conditions.

Long-term debt at 31 March 2008 and 2009 consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2008	2009	2009
Loans from banks and an insurance company			
due on varying dates through 2014 (*1)	¥ 3,185	¥ 3,152	\$ 32,085
Lease obligations	14	137	1,400
Less, portion of long-term loans	(630)	(150)	(1,525)
Less, current portion of lease obligations	(6)	(46)	(473)
	¥ 2,563	¥ 3,093	\$ 31,487

(\*1) The weighted average interest rates on loans from banks and an insurance company were as follows:

at 31 March 2008	2.1%
at 31 March 2009	2.1%

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

The aggregate annual maturities of long-term debt at 31 March 2009 are as follows:

	Millions of Yen	Thousands of U.S. Dollars
Years ending 31 March:		
2010	¥ 150	\$ 1,525
2011	1,820	18,526
2012	1,120	11,400
2013	45	456
2014	17	178
Total	¥ 3,152	\$ 32,085

The aggregate annual maturities of lease obligations subsequent to 31 March 2009 are as follows:

	Millions of Yen	Thousands of U.S. Dollars
Years ending 31 March:		
2010	¥ 46	\$ 473
2011	38	391
2012	29	291
2013	18	179
2014 and thereafter	6	66
Total	¥ 137	\$ 1,400

The Companies' assets amounting to ¥500 million and ¥500 million (\$5,090 thousand) pledged as collateral for long-term debt, including the current portion of long-term debt, at 31 March 2008 and 2009 are summarized as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2008	2009	2009
Investments in securities	¥ 884	¥ 912	\$ 9,285

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 8. Accrued severance indemnities

The Company has adopted a funded defined benefit plan covering all of its employees. The consolidated subsidiaries, excluding certain overseas subsidiaries, have adopted funded and/or unfunded defined benefit plans. In addition, the Companies may occasionally pay supplementary benefits to retired employees.

The Company and certain domestic consolidated subsidiaries revised a portion of their retirement benefits plans to defined benefits pension plan on 1 January 2009, and applied “Accounting for Transfer between Retirement Benefit Plans” (Accounting Standard Board of Japan Implementation Guidance No.1). This change was no impact on income for the year ended 31 March 2009.

The funded and accrued status of the Companies’ retirement benefit plans at 31 March 2008 and 2009 are summarized as follows:

	Millions of Yen		Thousands of
	2008	2009	U.S. Dollars
			2009
Projected benefit obligations	¥ 5,201	¥ 4,827	\$ 49,144
Unrecognized net actuarial losses	(436)	(579)	(5,896)
Unrecognized net retirement benefit obligation at transition	(605)	(519)	(5,281)
Plan assets at fair value	(3,890)	(3,398)	(34,594)
Prepaid pension cost	422	329	3,346
Accrued severance indemnities	¥ 692	¥ 660	\$ 6,719

Certain consolidated subsidiaries adopted simplified method in the calculation of their retirement benefit obligation.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

Net periodic pension cost related to the retirement benefits for the years ended 31 March 2007, 2008 and 2009 was as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2007	2008	2009	2009
Service cost	¥ 525	¥ 459	¥ 418	\$ 4,250
Interest cost	101	94	86	879
Expected return on plan assets	(61)	(62)	(53)	(535)
Amortization of net actuarial losses	82	70	110	1,116
Amortization of net retirement benefit obligation at transition	86	86	86	880
Net periodic pension cost	¥ 733	¥ 647	¥ 647	\$ 6,590

Net periodic pension cost for consolidated subsidiaries adopting the simplified method are included in "Service cost."

Pension benefit obligations are attributed to periods by the straight-line method over the estimated remaining years of service of the eligible employees.

Assumptions used in accounting for the above plans for the years ended 31 March 2007, 2008 and 2009 were as follows:

	2007	2008	2009
Discount rate	2.1%	2.1%	2.1%
Expected rate of return on plan assets	1.5%	1.5%	1.5%

### 9. Commitments and contingent liabilities

The Companies were contingently liable for outstanding discounted notes of ¥2,324 million and ¥2,517 million (\$25,619 thousand) at 31 March 2008 and 2009, respectively.

The Company provided guarantees to an intermediary trading company of ¥1,205 million and ¥1,243 million (\$12,651 thousand) for the collection of its accounts receivables from contracted sales agents/distributors at 31 March 2008 and 2009, respectively.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 10. Derivative financial instruments

(1) Status of transactions

a) Nature and purpose of transactions

The Companies enter into forward foreign exchange contracts to reduce the risk arising from exchange rate fluctuation in sales to and purchases from other countries denominated in foreign currencies conducted in the ordinary course of operations.

b) Policy for utilization of transactions

The Companies utilize foreign-currency-related derivative financial instruments within limits not exceeding the amounts of receivables and payables denominated in foreign currencies and contracted sales or purchase amounts and do not use them for speculative purposes.

c) Transaction risk

Counterparties, with whom the Companies enter into derivative financial instrument agreements, are highly creditworthy banks and, therefore, the Companies do not expect losses due to non-performance of the counterparties.

d) Risk management

Derivative transactions are executed and managed centrally by the Financing Group of the Tokyo Administration Department based on the concept of segregation of duties.

e) Other

The contract or notional amount shown in the “Summary of transactions” below is not indicative of the quantity of market risk.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### (2) Summary of transactions

The contract or notional amount and fair value of, and valuation gain or loss on, outstanding derivative positions at 31 March 2008 and 2009 are summarized as follows:

	Millions of Yen					
	2008			2009		
	Contract or notional amount	Fair value	Valuation gain (loss)	Contract or notional amount	Fair value	Valuation gain (loss)
Forward foreign exchange						
Contracts:						
Short-term:						
Sell USD and buy JPY	¥ 404	¥ 408	¥ (4)	¥ 308	¥ 297	¥ 11
Long-term:						
Buy USD and sell EUR	85	85	(0)	380	368	(12)
Buy SGD and sell EUR	—	—	—	173	175	2
Buy JPY and sell EUR	102	100	(2)	24	25	1
Buy GBP and sell EUR	60	57	(3)	—	—	—
Total			<u>¥ (9)</u>			<u>¥ 2</u>

	Thousands of U.S. Dollars		
	Contract or notional amount	Fair value	Valuation gain (loss)
Forward foreign exchange			
Contracts:			
Short-term:			
Sell USD and buy JPY	\$ 3,137	\$ 3,022	\$ 115
Long-term:			
Buy USD and sell EUR	3,872	3,748	(124)
Buy SGD and sell EUR	1,764	1,788	24
Buy JPY and sell EUR	253	259	6
Buy GBP and sell EUR			
Total			<u>\$ 21</u>

The fair value has been quoted from financial institutions with which the Companies enter into forward foreign exchange contracts.

Derivative financial instruments which qualify for hedge accounting under “Accounting Standard for Foreign Currency Transactions and Financial Statements” are excluded from the above disclosure.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 11. Cash dividends

(1) Dividends from retained earnings

The following appropriation of retained earnings applicable to the year ended 31 March 2006 was approved at an annual general shareholders' meeting held on 29 June 2006:

- (1) Total amount of dividends: ¥516 million
- (2) Dividends per share: ¥7.50
- (3) Record date: 31 March 2006
- (4) Effective date: 30 June 2006

The following appropriation of retained earnings applicable to the year ended 31 March 2007 was approved at an annual general shareholders' meeting held on 28 June 2007:

- (1) Total amount of dividends: ¥688 million
- (2) Dividends per share: ¥10.00
- (3) Record date: 31 March 2007
- (4) Effective date: 29 June 2007

The following appropriation of retained earnings applicable to the year ended 31 March 2008 was resolved by the board of directors on 31 October 2007:

- (1) Total amount of dividends: ¥413 million
- (2) Dividends per share: ¥6.00
- (3) Record date: 30 September 2007
- (4) Effective date: 4 December 2007

The following appropriation of retained earnings applicable to the year ended 31 March 2008 was approved at an annual general shareholders' meeting held on 26 June 2008:

- (1) Total amount of dividends: ¥482 million
- (2) Dividends per share: ¥7.00
- (3) Record date: 31 March 2008
- (4) Effective date: 27 June 2008

The following appropriation of retained earnings applicable to the year ended 31 March 2009 was resolved by the board of directors on 31 October 2008:

- (1) Total amount of dividends: ¥413 million
- (2) Dividends per share: ¥6.00
- (3) Record date: 30 September 2008
- (4) Effective date: 2 December 2008

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

- (2) Dividends whose effective date is after the end of the current fiscal year and whose record date is in the current fiscal year

The following appropriation of retained earnings which has not been reflected in the accompanying consolidated financial statements for the year ended 31 March 2007 was approved at an annual general shareholders' meeting held on 28 June 2007:

- (1) Total amount of dividends: ¥688 million
- (2) Source of dividends: Retained earnings
- (3) Dividends per share: ¥10.00
- (4) Record date: 31 March 2007
- (5) Effective date: 29 June 2007

The following appropriation of retained earnings which has not been reflected in the accompanying consolidated financial statements for the year ended 31 March 2008 was approved at an annual general shareholders' meeting held on 26 June 2008:

- (1) Total amount of dividends: ¥482 million
- (2) Source of dividends: Retained earnings
- (3) Dividends per share: ¥7.00
- (4) Record date: 31 March 2008
- (5) Effective date: 27 June 2008

The following appropriation of retained earnings which has not been reflected in the accompanying consolidated financial statements for the year ended 31 March 2009 was approved at an annual general shareholders' meeting held on 25 June 2009:

- (1) Total amount of dividends: ¥481 million
- (2) Source of dividends: Retained earnings
- (3) Dividends per share: ¥7.00
- (4) Record date: 31 March 2009
- (5) Effective date: 26 June 2009

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 12. Revaluation of land

Effective 31 March 2000, the Company revalued its land used for operations in accordance with the Law Concerning the Revaluation of Land (Law No. 34 promulgated on 31 March 1998 which was partially amended on 31 March 1999).

The tax effect of the revaluation difference is recorded as “Deferred tax liabilities on revaluation of land” under non-current liabilities and the revaluation gain, net of taxes, is reported as a component of valuation, translation adjustments and other under net assets. The fair value of the revalued land at 31 March 2008 and 2009 was lower than the carrying amount of such land after revaluation by ¥5,772 million and ¥4,982 million (\$50,714 thousand), respectively.

Two overseas subsidiaries revalued their land in accordance with the applicable local regulations and accounting standards. The revaluations resulted in gain and the related tax effects of ¥18 million were included in “Deferred tax liabilities on revaluation of land” under non-current liabilities, and ¥7 million were included in “Minority interests” and the remaining after-tax amounts of ¥47 million were included in “Revaluation gain on land” under net assets at 31 March 2008.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 13. Selling, General and Administrative Expenses

	Millions of Yen			Thousands of U.S. Dollars
	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2009</u>
Depreciation	¥ 272	¥ 301	¥ 432	\$ 4,397
Provision of allowance for doubtful accounts	133	145	117	1,196
Provision for bonuses	53	36	62	632
Retirement benefit expenses	449	476	459	4,677
Directors' compensations and Employees' salaries and bonuses	5,887	6,365	6,419	65,345
Transportation expenses	3,370	3,827	3,780	38,481
Sales commission	1,877	2,174	2,009	20,454
Provision for directors' retirement benefits	23	-	-	-
Provision for product warranties	92	-	-	-
Other	6,241	7,281	7,364	74,962
<b>Total</b>	<b>¥ 18,397</b>	<b>¥ 20,605</b>	<b>¥ 20,642</b>	<b>\$ 210,144</b>

Research and development cost included in "Selling, general and administrative expenses" and manufacturing costs for the years ended 31 March 2007, 2008 and 2009 amounted to ¥ 1,496 million, ¥ 1,605 million and ¥ 1,800 million (\$18,326 thousand), respectively.

### 14. Supplementary cash flow information

Cash and cash equivalents at 31 March 2008 and 2009 consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	<u>2008</u>	<u>2009</u>	<u>2009</u>
Cash on hand and in banks	¥ 7,976	¥ 8,625	\$ 87,807
Less, time deposits with deposit term of over three months	(118)	(33)	(339)
<b>Cash and cash equivalents</b>	<b>¥ 7,858</b>	<b>¥ 8,592</b>	<b>\$ 87,468</b>

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 15. Income taxes

The Companies are subject to several taxes based on income, which in the aggregate, resulted in a statutory tax rate of approximately 40.5% for the years ended 31 March 2007, 2008 and 2009.

Significant components of deferred tax assets and liabilities at 31 March 2008 and 2009 were as follows:

	Millions of Yen		Thousands of U.S. Dollars
	2008	2009	2009
Deferred tax assets:			
Accrued severance indemnities	¥ 232	¥ 218	\$ 2,216
Accrued directors' and corporate auditors' retirement benefits	140	132	1,339
Write-downs of investments in securities	167	147	1,492
Write-downs of golf membership and excess provision for allowance for doubtful accounts	36	33	337
Accrued bonuses	268	269	2,742
Accrued enterprise tax	101	34	345
Foreign tax credit	18	24	247
Tax loss carryforwards	85	55	566
Others	488	595	6,063
Gross deferred tax assets	<u>1,535</u>	<u>1,507</u>	<u>15,347</u>
Less, valuation allowance	<u>(171)</u>	<u>(145)</u>	<u>(1,480)</u>
Total deferred tax assets	<u>1,364</u>	<u>1,362</u>	<u>13,867</u>
Deferred tax liabilities:			
Net unrealized gain on securities	(834)	(4)	(39)
Prepaid pension cost	(171)	(133)	(1,355)
Others	(51)	(36)	(370)
Total deferred tax liabilities	<u>(1,056)</u>	<u>(173)</u>	<u>(1,764)</u>
Net deferred tax assets (liabilities)	<u>¥ 308</u>	<u>¥ 1,189</u>	<u>\$ 12,103</u>

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

A reconciliation of the statutory tax rate to the effective tax rates for the years ended 31 March 2007, 2008 and 2009 is as follows:

	2007	2008	2009
Statutory tax rate	40.5%	40.5%	40.5%
Increase (decrease) in taxes resulting from:			
Difference in statutory tax rates between parent and subsidiaries	(27.0)	(26.9)	(14.9)
Entertainment and other non-deductible expenses	3.4	3.0	3.2
Dividend income and other non-taxable amounts	(1.8)	(1.5)	(1.7)
Dividends from retained earnings	14.6	20.4	10.2
Decrease in valuation allowance of deferred tax assets	0.2	0.2	(2.5)
Income tax refund	—	(1.9)	(2.1)
Prior year's income taxes	—	2.2	—
Special tax credit for research and development, etc.	(0.1)	(1.8)	(1.7)
Foreign tax credit	(4.2)	(4.2)	(2.9)
Others	0.2	(1.0)	(2.3)
Effective tax rates	25.8%	29.0%	25.8%

### 16. Loss on impairment of fixed assets

The Companies review their fixed assets for impairment by grouping their operating assets by management accounting unit and grouping their rental assets and idle assets by individual unit. The Companies recognized the following loss on impairment of fixed assets for the year ended 31 March 2007:

Use	Item	Location
Idle properties	Machinery, etc.	Hiroshima

The above asset is a private electricity generator. This generator was utilized during the previous fiscal year, but its use was halted because of an increase in the costs of operation and maintenance during the year. As a result, this generator was deemed to be obsolete and a recovery of its fair value to book value was not deemed probable. Consequently, the Companies recognized loss on impairment of fixed assets.

The components of the loss on impairment recognized in the accompanying consolidated statement of income for the years ended 31 March 2007, 2008 and 2009 were as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2007	2008	2009	2009
Property, plant and equipment	¥ 11	¥ —	¥ —	\$ —

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### 17. Segment information

The Companies primarily operate in two business segments: “Paints” (selling paints, contract painting works and painting technical assistance) and “Other.” This segmentation is based on similarities in terms of the type, nature and selling methods of the products and among others.

Major products of each business segment are summarized as follows:

Business segment	Major products
Paints	Marine paints, synthetic resin paints, thinner and other paints, contracted painting works, painting technical assistance
Other	Rent and management of real estate, development of computer software, financial services, operation of golf practice range

The Companies also operate in three geographic areas “Domestic,” “Asia” and “Other.”

Geographical segments are based on geographical proximity.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

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Summarized financial information concerning the business and geographic segments in which the Companies operated for the years ended 31 March 2007, 2008 and 2009 is presented in the following tables:

### Business segments

	Millions of Yen									
	2007					2008				
	Paints	Other	Total	Eliminations or corporate	Consolidated	Paints	Other	Total	Eliminations or corporate	Consolidated
Net sales										
External sales	¥87,534	¥633	¥88,197	¥ -	¥88,197	¥104,208	¥591	¥104,799	¥ -	¥104,799
Intersegment sales or transfers	-	396	396	(396)	-	-	397	397	(397)	-
Total	87,534	1,059	88,593	(396)	88,197	104,208	988	105,196	(397)	104,799
Operating expenses (a)	79,482	694	80,176	763	80,939	95,014	650	95,664	1,003	96,667
Operating income	¥8,052	¥365	¥8,417	¥(1,159)	¥7,258	¥9,194	¥338	¥9,532	¥(1,400)	¥8,132
Total assets (b)	¥90,461	¥6,354	¥96,815	¥5,243	¥102,059	¥86,610	¥6,395	¥93,005	¥5,546	¥98,551
Depreciation and amortization	1,137	64	1,201	32	1,233	1,359	54	1,413	45	1,458
Capital expenditure	2,582	13	2,595	77	2,672	2,352	12	2,364	238	2,602

  

	2009									
	Millions of Yen					Thousands of U.S. Dollars				
	Paints	Other	Total	Eliminations or corporate	Consolidated	Paints	Other	Total	Eliminations or corporate	Consolidated
Net sales										
External sales	¥103,113	¥510	¥103,623	¥ -	¥103,623	\$1,049,712	\$5,187	\$1,054,899	\$ -	\$1,054,899
Intersegment sales or transfers	10	397	407	(407)	-	101	4,039	4,140	(4,140)	-
Total	103,123	907	104,030	(407)	103,623	1,049,813	9,226	1,059,039	(4,140)	1,054,899
Operating expenses (a)	93,470	630	94,100	1,093	95,193	951,546	6,408	957,954	11,130	969,084
Operating income	¥9,653	¥277	¥9,930	¥(1,500)	¥8,430	\$98,267	\$2,818	\$101,085	\$(15,270)	\$85,815
Total assets (b)	¥82,211	¥4,698	¥86,909	¥4,867	¥91,776	\$836,922	\$47,833	\$884,755	\$49,543	\$934,298
Depreciation and amortization	1,386	44	1,430	126	1,556	14,107	443	14,550	1,285	15,835
Capital expenditure	2,755	10	2,765	280	3,045	28,043	101	28,144	2,853	30,997

- (a) Expenses which are not attributable to any business segments represent primarily expenses incurred at the Company's administration department and included in "Elimination or Corporate" column. Such expenses amounted to ¥1,159 million, ¥1,400 million and ¥1,500 million (\$15,270 thousand) for the years ended 31 March 2007, 2008 and 2009, respectively.
- (b) Corporate assets, which are included in "Elimination or Corporate" column, are comprised primarily of cash, investments in securities held by the Company and other assets held at its administration department. The balances of those assets were ¥5,281 million, ¥5,635 million and ¥4,938 million (\$50,266 thousand) at 31 March 2007, 2008 and 2009, respectively.
- (c) As described in Note 2 (9), effective the year ended 31 March 2008, the Company and its domestic consolidated subsidiaries changed their depreciation method for property, plant and equipment acquired on or after 1 April 2007 as stipulated by the amended Corporation Tax Law. As a result, operating expenses of "Paints" increased by ¥23 million and "Other" increased by ¥3 million, and accordingly, operating income decreased by the same amount, compared with the amount under the previous method. In addition, the residual values (5% of the acquisition cost) of the property, plant and equipment acquired on or before 31 March 2007 which were fully depreciated based on the Corporation Tax Law before the amendment are depreciated equally over five years starting from the year ended 31 March 2008. As a result, operating expenses of "Paints" increased by ¥54 million and "Other" increased by ¥5 million, and accordingly, operating income decreased by the same amount, compared with the amounts under the previous method.
- (d) As described in Note 2 (8), the Company adopted "Accounting Standard for Measurement of Inventories" (ASBJ Statement No. 9, issued on 5 July 2006) effective the year ended 31 March 2009. For the year ended 31 March 2009, the change of this accounting policy resulted in decrease of operating income in "Paints" by ¥33 million (\$340 thousand), compared with the amounts under the previous method.
- (e) As described in Note 2 (9), effective the year ended 31 March 2009, pursuant to an amendment to the Corporation Tax Law, the Company and its domestic consolidated subsidiaries have reviewed the useful lives of machinery and equipment and their classification of assets. As a result, operating income in "Paints" decreased by ¥19 million (\$197 thousand), compared with the amounts under the previous method.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

31 March 2007, 2008, 2009

### Geographical segments

	Millions of Yen											
	2007						2008					
	Domestic	Asia (c)	Other (d)	Total	Eliminations or corporate	Consolidated	Domestic	Asia (c)	Other (d)	Total	Eliminations or corporate	Consolidated
Net sales												
External sales	¥35,334	¥43,744	¥9,119	¥88,197	¥ –	¥88,197	¥39,623	¥54,021	¥11,155	¥104,799	¥ –	¥104,799
Intersegment sales or transfers	6,945	6,554	677	14,177	(14,177)	–	7,211	7,558	960	15,729	(15,729)	–
Total	42,279	50,298	9,796	102,374	(14,177)	88,197	46,834	61,579	12,115	120,528	(15,729)	104,799
Operating expenses (a)	40,898	44,528	10,390	95,816	(14,877)	80,939	44,843	55,869	12,404	113,116	(16,449)	96,667
Operating income (loss)	¥1,381	¥5,770	¥(594)	¥6,558	¥ 700	¥7,258	¥1,991	¥5,710	¥(289)	¥7,412	¥ 720	¥8,132
Total assets (b)	¥62,749	¥46,264	¥9,005	¥118,018	¥(15,959)	¥102,059	¥61,709	¥43,970	¥8,901	¥114,580	¥(16,029)	¥98,551

  

	2009											
	Millions of Yen						Thousands of U.S. Dollars					
	Domestic	Asia (c)	Other (d)	Total	Eliminations or corporate	Consolidated	Domestic	Asia (c)	Other (d)	Total	Eliminations or corporate	Consolidated
Net sales												
External sales	¥43,579	¥49,205	¥10,839	¥103,623	¥ –	¥103,623	\$443,644	\$500,919	\$110,336	\$1,054,899	\$ –	\$1,054,899
Intersegment sales or transfers	6,718	8,382	815	15,915	(15,915)	–	68,387	85,335	8,297	162,019	(162,019)	–
Total	50,297	57,587	11,654	119,538	(15,915)	103,623	512,031	586,254	118,633	1,216,918	(162,019)	1,054,899
Operating expenses (a)	47,304	52,497	12,005	111,806	(16,613)	95,193	481,562	534,427	122,213	1,138,202	(169,118)	969,084
Operating income (loss)	¥2,993	¥5,090	¥(351)	¥7,732	¥698	¥8,430	\$30,469	\$51,827	\$(3,580)	\$78,716	\$7,099	\$85,815
Total assets (b)	¥60,296	¥41,909	¥7,170	¥109,375	¥(17,599)	¥91,776	\$613,824	\$426,648	\$72,991	\$1,113,463	\$(179,165)	\$934,298

- (a) Expenses which are not attributable to any industry segments represent primarily expenses incurred at the Company's administration department and included in "Elimination or Corporate" column. Such expenses amounted to ¥1,159 million, ¥1,400 million and ¥1,500 million (\$15,270 thousand) for the years ended 31 March 2007, 2008 and 2009, respectively.
- (b) Corporate assets, which are included in "Elimination or Corporate" column, are comprised primarily of cash, investments in securities held by the Company and other assets held at its administration department. Balances of those assets were ¥5,281 million, ¥5,635 million and ¥4,938 million (\$50,266 thousand) at 31 March 2007, 2008 and 2009, respectively.
- (c) Primarily included are China, Singapore, Hong Kong, Korea, Taiwan, Thailand, Malaysia and Indonesia.
- (d) Primarily included are the Netherlands, U.S.A. and U.K.
- (e) As described in Note 2 (9), effective the year ended 31 March 2008, the Company and its domestic consolidated subsidiaries changed their depreciation method for property, plant and equipment acquired on or after 1 April 2007 as stipulated by the amended Corporation Tax Law. As a result, operating expenses of "Domestic" increased by ¥27 million and accordingly, operating income decreased by the same amount, compared with the amount under the previous method. In addition, the residual values (5% of the acquisition cost) of the property, plant and equipment acquired on or before 31 March 2007 which were fully depreciated based on the Corporation Tax Law before the amendment are depreciated equally over five years starting from the year ended 31 March 2008. As a result, operating expenses of "Domestic" increased by ¥60 million and accordingly, operating income decreased by the same amount, compared with the amounts under the previous method.
- (f) As described in Note 2 (8), the Company adopted "Accounting Standard for Measurement of Inventories" (ASBJ Statement No. 9, issued on 5 July 2006) effective the year ended 31 March 2009. For the year ended 31 March 2009, the change of this accounting policy resulted in decrease of operating income in "Domestic" by ¥33 million (\$340 thousand), compared with the amounts under the previous method.
- (g) As described in Note 2 (9), effective the year ended 31 March 2009, pursuant to an amendment to the Corporation Tax Law, the Company and its domestic consolidated subsidiaries have reviewed the useful lives of machinery and equipment and their classification of assets. As a result, operating income in "Domestic" decreased by ¥19 million (\$197 thousand), compared with the amounts under the previous method.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

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Overseas and export sales for the years ended 31 March 2007, 2008 and 2009 are summarized as follows:

	Millions of Yen			Thousands of U.S. Dollars
	2007	2008	2009	2009
Overseas and export sales:				
Asia (a)	¥ 43,695	¥ 53,965	¥ 49,173	\$ 500,590
Other (b)	9,166	11,223	10,895	110,910
	¥ 52,861	¥ 65,188	¥ 60,068	\$ 611,500
 Consolidated net sales	 ¥ 88,197	 ¥ 104,799	 ¥ 103,623	 \$ 1,054,899
 Percentage of overseas and exports sales to consolidated net sales:	 2007	 2008	 2009	
Asia (a)	49.5%	51.5%	47.5%	
Other (b)	10.4%	10.7%	10.5%	
	59.9%	62.2%	58.0%	

(a) Primarily included are China, Singapore, Hong Kong, Korea, Taiwan, Thailand, Malaysia, Indonesia and Oceania.

(b) Primarily included are the Netherlands, U.S.A., U.K and Africa.

Overseas and export sales represent the total amount of export sales of the Company and domestic subsidiaries and sales of the overseas subsidiaries.

# CHUGOKU MARINE PAINTS, LTD. AND ITS SUBSIDIARIES

## Notes to Consolidated Financial Statements

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### 18. Merger of consolidated subsidiaries

#### (1) Outline of the merger

##### a) Companies involved in the merger and principal business activities

CHUGOKU PAINTS B.V.

Paints: Production and sales of paints

FIJNAART HOLDINGS B.V.

Paints: Management control of consolidated subsidiaries in Europe

CHUGOKU COATINGS B.V.

Paints: Inactive Company

##### b) Purpose of the merger

This merger aims to enhance the business efficiency of consolidated subsidiaries in Europe.

##### c) Date: 18 August 2008

##### d) Method of the merger

CHUGOKU PAINTS B.V., as the surviving company, acquired FIJNAART HOLDINGS B.V. and CHUGOKU COATINGS B.V., which were subsequently dissolved.

#### (2) Summary of accounting procedures

The merger is accounted for as a common control transaction, based on “Accounting Standard for Business Combinations” (Issued by the Business Accounting Council in Japan on 31 October 2003).