

**KYOKUTO KOWA CORPORATION**

*Financial Statements  
for the Year Ended March 31, 2016  
and Independent Auditor's Report*

## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of KYOKUTO KOWA CORPORATION:

We have audited the accompanying balance sheet of KYOKUTO KOWA CORPORATION as of March 31, 2016, and the related statements of income, and changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory information, all expressed in Japanese yen.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Companies Act of Japan and applicable regulations and accounting principles generally accepted in Japan, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of KYOKUTO KOWA CORPORATION as of March 31, 2016, and the results of its operations for the year then ended in accordance with the Companies Act of Japan and applicable regulations and accounting principles generally accepted in Japan.

### Emphasis of Matter

As explained in Note 1 to the financial statements, the information provided in the notes to the financial statements is limited to that required by the Companies Act of Japan and applicable regulations.

Statements of comprehensive income and cash flows are not required as a part of the basic financial statements under the Companies Act of Japan and applicable regulations and, accordingly, are not presented herein. Our opinion is not modified in respect of these matters.

### Convenience Translation

Our audit also comprehended the translation of Japanese yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made in accordance with the basis stated in Note 1 to the financial statements. Such U.S. dollar amounts are presented solely for the convenience of readers outside Japan.

*Deloitte Touche Tohmatsu LLC*

May 19, 2016

**KYOKUTO KOWA CORPORATION**  
**Balance Sheet**  
**March 31, 2016**

<u>ASSETS</u>	<u>Millions of Yen</u> 2016	<u>Thousands of U.S. Dollars (Note 1)</u> 2016	<u>LIABILITIES AND EQUITY</u>	<u>Millions of Yen</u> 2016	<u>Thousands of U.S. Dollars (Note 1)</u> 2016
<b>CURRENT ASSETS:</b>			<b>CURRENT LIABILITIES:</b>		
Cash and cash equivalents (Note 7)	¥ 399	\$ 3,541	Current portion of long-term loans (Note 7)	¥ 43	\$ 382
Receivables (Notes 7 and 8):			Payables (Notes 7 and 8):		
Trade notes	152	1,349	Trade notes	782	6,940
Trade accounts	3,151	27,964	Electronically recorded obligations	905	8,032
Parent company and affiliated companies (Note 8)	844	7,490	Trade accounts	1,513	13,427
Other	133	1,180	Parent company and affiliated companies (Note 8)	101	896
Inventories (Note 3.a)	624	5,538	Other	76	674
Deferred tax assets (Note 6)	77	684	Income taxes payable (Note 7)	16	142
Prepaid expenses and other current assets	9	80	Advances received on uncompleted construction contracts (Note 7)	1,280	11,360
Total current assets	<u>5,389</u>	<u>47,826</u>	Allowance for losses on construction contracts	38	337
			Provision for warranties for completed construction	58	515
			Other current liabilities	<u>208</u>	<u>1,846</u>
			Total current liabilities	<u>5,020</u>	<u>44,551</u>
<b>PROPERTY, PLANT AND EQUIPMENT:</b>			<b>LONG-TERM LIABILITIES:</b>		
Land (Note 3.b)	926	8,218	Long-term loans (Note 7)	26	231
Buildings and structures (Note 3.b)	1,891	16,782	Other	<u>28</u>	<u>248</u>
Machinery and equipment (Note 3.b)	2,132	18,921	Total long-term liabilities	<u>54</u>	<u>479</u>
Tools, furniture and fixtures	<u>958</u>	<u>8,502</u>			
Total	5,907	52,423	<b>Total liabilities</b>	5,074	45,030
Accumulated depreciation	<u>(4,392)</u>	<u>(38,978)</u>	<b>CONTINGENT LIABILITIES (Note 3.c)</b>		
Net property, plant and equipment	<u>1,515</u>	<u>13,445</u>	<b>EQUITY (Notes 4, 5, and 9):</b>		
			Common stock—authorized, 30,000,000 shares; issued, 8,620,000 shares in 2016	100	888
<b>INVESTMENTS AND OTHER ASSETS:</b>			Capital surplus:		
Investment securities (Note 7)	58	515	Additional paid-in capital	195	1,731
Deferred tax assets (Note 6)	11	98	Other capital surplus	812	7,206
Other assets (Note 8)	183	1,624	Retained earnings:		
Allowance for doubtful accounts	<u>(18)</u>	<u>(160)</u>	Legal reserve	118	1,047
Total investments and other assets	234	2,077	Unappropriated	835	7,411
			Unrealized gain on available-for-sale securities	4	35
			Total equity	2,064	18,318
<b>TOTAL</b>	<u>¥ 7,138</u>	<u>\$ 63,348</u>	<b>TOTAL</b>	<u>¥ 7,138</u>	<u>\$ 63,348</u>

See notes to financial statements.

**KYOKUTO KOWA CORPORATION**  
**Statement of Income**  
**Year Ended March 31, 2016**

	<u>Millions of Yen</u> 2016	<u>Thousands of U.S. Dollars</u> (Note 1) 2016
NET SALES (Note 8)	¥ 14,602	\$ 129,588
COST OF SALES (Note 8)	<u>13,144</u>	<u>116,649</u>
Gross profit	1,458	12,939
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES (Note 8)	<u>1,346</u>	<u>11,945</u>
Operating income	<u>112</u>	<u>994</u>
OTHER INCOME (EXPENSES) (Note 8):		
Interest and dividend income	2	18
Royalty income	6	53
Interest expense	( 2)	( 18)
Financing expenses	( 10)	( 88)
Other—net	<u>( 1)</u>	<u>( 9)</u>
Other expenses—net	<u>( 5)</u>	<u>(44)</u>
INCOME BEFORE INCOME TAXES	<u>107</u>	<u>950</u>
INCOME TAXES (Note 6):		
Current	40	355
Deferred	<u>40</u>	<u>355</u>
Total income taxes	<u>80</u>	<u>710</u>
NET INCOME	<u>¥ 27</u>	<u>\$ 240</u>
	<u>Yen</u>	<u>U.S. Dollars</u>
PER SHARE OF COMMON STOCK (Notes 4 and 9):		
Basic net income	¥ 3.20	\$ 0.03
Cash dividends applicable to the year	24.00	0.21

See notes to financial statements.

**KYOKUTO KOWA CORPORATION**  
**Statement of Changes in Equity**  
**Year Ended March 31, 2016**

	Thousands	Millions of Yen						
	Outstanding	Common	Capital Surplus		Retained Earnings		Unrealized Gain on Available- for-Sale Securities	Total Equity
	Number of Shares of Common Stock		Stock	Additional Paid-In Capital	Other Capital Surplus	Legal Reserve		
BALANCE, MARCH 31, 2015	8,620	¥ 100	¥ 195	¥ 812	¥ 118	¥ 1,015	¥ 3	¥ 2,243
Net income						27		27
Cash dividends, ¥24 per share						(207)		(207)
Net change in the year							1	1
BALANCE, MARCH 31, 2016	8,620	¥ 100	¥ 195	¥ 812	¥ 118	¥ 835	¥ 4	¥ 2,064

	Thousands of U.S. Dollars (Note 1)							
	Common Stock	Capital Surplus		Retained Earnings		Unrealized Gain on Available- for-Sale Securities	Total Equity	
		Paid-In Capital	Other Capital Surplus	Legal Reserve	Unappropri- -ated			
BALANCE, MARCH 31, 2015	\$ 888	\$ 1,731	\$ 7,206	\$ 1,047	\$ 9,008	\$ 26	\$ 19,906	
Net income					240		240	
Cash dividends, \$0.21 per share					(1,837)		(1,837)	
Net change in the year						9	9	
BALANCE, MARCH 31, 2016	\$ 888	\$ 1,731	\$ 7,206	\$ 1,047	\$ 7,411	\$ 35	\$ 18,318	

See notes to financial statements.

**KYOKUTO KOWA CORPORATION**  
**Notes to Financial Statements**  
**Year Ended March 31, 2016**

---

**1. BASIS OF PRESENTATION OF FINANCIAL STATEMENTS**

The accompanying financial statements have been prepared from the accounts maintained by KYOKUTO KOWA CORPORATION (the "Company"), in accordance with the provisions set forth in the Companies Act of Japan and applicable regulations and in accordance with accounting principles generally accepted in Japan. The information provided in the notes to the financial statements is limited to that required by the Companies Act of Japan and applicable regulations. Statements of comprehensive income and cash flows are not required as a part of the basic financial statements under the Companies Act of Japan and applicable regulations and, accordingly, are not presented herein.

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

The financial statements are stated in Japanese yen, the currency of the country in which the Company is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥112.68 to \$1, the approximate rate of exchange at March 31, 2016. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

- a. Inventories**—Construction projects in progress, finished products, and work in process are stated at cost as determined by the specific identification method. Raw materials and supplies are stated at cost as determined by the moving-average method. The write-downs of inventories due to decreased profitability are reflected in the valuation of raw materials and supplies and the accompanying loss is recognized as cost of goods sold, in principle.
- b. Property, Plant and Equipment**—Property, plant and equipment are stated at cost. Depreciation is computed by the declining-balance method based on the estimated useful lives of the assets, while the straight-line method is applied to the buildings, excluding building fixtures, acquired on or after April 1, 1998. The range of useful lives is principally from 12 to 38 years for buildings and structures and from 3 to 9 years for machinery and equipment and tools, furniture and fixtures.
- c. Long-Lived Assets**—The Company reviews its long-lived assets for impairment whenever events or changes in circumstance indicate the carrying amount of an asset or asset group may not be recoverable. An impairment loss would be recognized if the carrying amount of an asset or asset group exceeds the sum of the undiscounted future cash flows expected to result from the continued use and eventual disposition of the asset or asset group. The impairment loss would be measured as the amount by which the carrying amount of the asset exceeds its recoverable amount, which is the higher of the discounted cash flows from the continued use and eventual disposition of the asset or the net selling price at disposition.
- d. Investment Securities**—Investment securities are classified and accounted for, depending on management's intent, as available-for-sale securities. They are reported at fair value, with unrealized gains and losses, net of applicable taxes, reported in a separate component of equity.

Nonmarketable available-for-sale securities are stated at cost determined by the moving-average method. For other-than-temporary declines in fair value, investment securities are reduced to net realizable value by a charge to income.

- e. **Allowance for Doubtful Accounts**—The allowance for doubtful accounts is provided for at an amount sufficient to cover possible losses on collection. It consists of the estimated uncollectible amount with respect to identified doubtful receivables and an amount calculated by applying the percentage of actual losses on collection experienced in the past to remaining receivables.
- f. **Allowance for Losses on Construction Contract**—To cover losses which have a high probability of occurring in the future upon work completion, an allowance for estimated losses is provided based on the amount of orders received and the estimated cost.
- g. **Provision for Warranties for Completed Construction**—Provision for warranties for completed construction is provided for anticipated future costs within the warranty period arising from warranties on completed construction.
- h. **Construction Contracts**— In December 2007, the Accounting Standards Board of Japan (ASBJ) issued ASBJ Statement No. 15 "Accounting Standard for Construction Contracts," and ASBJ Guidance No. 18 "Guidance on Accounting Standard for Construction Contracts," Under this accounting standard, construction revenue and construction costs should be recognized by the percentage-of-completion method if the outcome of a construction contract can be estimated reliably. When total construction revenue, total construction costs and the stage of completion of the contract at the balance sheet date can be reliably measured, the outcome of a construction contract is deemed to be estimated reliably. If the outcome of a construction contract cannot be reliably estimated, the completed-contract method should be applied. When it is probable that the total construction costs will exceed total construction revenue, an estimated loss on the contract should be immediately recognized by providing for a loss on construction contracts.

The revenues recognized by the percentage-of-completion method for the year ended March 31, 2016, were ¥8,868 million (\$78,701 thousand).

- i. **Income Tax**—The provision for income taxes is computed based on the pretax income included in the statement of income. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities. Deferred taxes are measured by applying currently enacted income tax rates to the temporary differences.

The Company's parent company files a tax return under the consolidated corporate tax system, which allows companies to base tax payments on the combined profits or losses of the parent company and its wholly owned domestic subsidiaries. The Company is included in the consolidated corporate tax system.

- j. **Per Share Information**—Basic net income per share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding for the period.

Cash dividends per share presented in the accompanying statement of income are dividends applicable to the fiscal year, including dividends to be paid after the end of the year.

### 3. NOTES TO BALANCE SHEET

#### *a. Inventories*

Inventories at March 31, 2016, consisted of the following:

	Millions of Yen	Thousands of U.S. Dollars
	2016	2016
Construction projects in progress	¥ 193	\$ 1,713
Finished products	328	2,911
Work in process	38	337
Raw materials and supplies	65	577
Total	<u>¥ 624</u>	<u>\$ 5,538</u>

#### *b. Pledged assets*

	Millions of Yen	Thousands of U.S. Dollars
	2016	2016
Assets pledged as collateral:		
Land	¥ 853	\$ 7,570
Buildings and structures	419	3,719
Machinery and equipment	28	248
Total	<u>¥ 1,300</u>	<u>\$ 11,537</u>

The following assets, which are included above, are pledged as factory foundation collateral:

Land	¥ 853	\$ 7,570
Buildings and structures	328	2,911
Machinery and equipment	28	248
Total	<u>¥ 1,209</u>	<u>\$ 10,729</u>

The Company pledged the above assets as collateral to secure the following parent company's bank loans.

Secured liabilities:

Loans from banks of parent company	¥ 1,978	\$ 17,554
------------------------------------	---------	-----------

#### *c. Contingent liabilities*

	Millions of Yen	Thousands of U.S. Dollars
	2016	2016
Guarantees to loans from banks of parent company	¥ 1,308	\$ 11,608
Trade notes endorsed	159	1,411
Total	<u>¥ 1,467</u>	<u>\$ 13,019</u>



#### 4. NOTES TO STATEMENT OF CHANGES IN EQUITY

##### *a. Type and number of outstanding shares*

Type of shares	Number of Shares			
	Balance at Beginning of Year	Increase in Shares During the Year	Decrease in Shares During the Year	Balance at End of Year
Issued stock:				
Common stock	8,620,000	—	—	8,620,000

##### *b. Dividends*

###### (1) Dividends paid to shareholders

For the year ended March 31, 2016

Resolution Approved by	Type of Shares	Amount		Amount per Share		Record Date	Effective Date
		Millions of Yen	Thousands of U.S. Dollars	Yen	U.S. Dollars		
Annual General Meeting of Shareholders (June 24, 2015)	Common stock	¥103	\$914	¥12	\$0.11	March 31, 2015	June 25, 2015
Board of Directors (October 20, 2015)	Common stock	¥103	\$914	¥12	\$0.11	September 30, 2015	November 30, 2015

###### (2) Dividends with a record date during the fiscal year but an effective date subsequent to the fiscal year

For the year ended March 31, 2016

Resolution Approved by	Type of Shares	Amount		Amount per Share		Record Date	Effective Date
		Millions of Yen	Thousands of U.S. Dollars	Yen	U.S. Dollars		
Annual General Meeting of Shareholders (June 23, 2016)	Common stock	¥103	\$914	¥12	\$0.11	March 31, 2016	June 24, 2016

#### 5. EQUITY

Japanese companies are subject to the Companies Act of Japan (the "Companies Act"). The significant provisions in the Companies Act that affect financial and accounting matters are summarized below:

### *a. Dividends*

Under the Companies Act, companies can pay dividends at any time during the fiscal year in addition to the year-end dividend upon resolution at the shareholders' meeting. For companies that meet certain criteria including (1) having a Board of Directors, (2) having independent auditors, (3) having an Audit & Supervisory Board, and (4) the term of service of the directors being prescribed as one year rather than the normal two-year term by its articles of incorporation, the Board of Directors may declare dividends (except for dividends-in-kind) at any time during the fiscal year if the company has prescribed so in its articles of incorporation. However, the Company cannot do so because it does not meet all the above criteria.

Semiannual interim dividends may also be paid once a year upon resolution by the Board of Directors if the articles of incorporation of the company so stipulate. The Companies Act provides certain limitations on the amounts available for dividends or the purchase of treasury stock. The limitation is defined as the amount available for distribution to the shareholders, but the amount of net assets after dividends must be maintained at no less than ¥3 million.

### *b. Increases/Decreases and Transfer of Common Stock, Reserve and Surplus*

The Companies Act requires that an amount equal to 10% of dividends must be appropriated as a legal reserve (a component of retained earnings) or as additional paid-in capital (a component of capital surplus), depending on the equity account charged upon the payment of such dividends, until the aggregate amount of legal reserve and additional paid-in capital equals 25% of the common stock. Under the Companies Act, the total amount of additional paid-in capital and legal reserve may be reversed without limitation. The Companies Act also provides that common stock, legal reserve, additional paid-in capital, other capital surplus and retained earnings can be transferred among the accounts within equity under certain conditions upon resolution of the shareholders.

## 6. INCOME TAXES

The tax effects of significant temporary differences which resulted in deferred tax assets and liabilities at March 31, 2016, are as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2016	2016
Deferred tax assets:		
Allowance for losses on construction contracts	¥ 13	\$ 116
Provision for warranties for completed construction	20	178
Allowance for doubtful accounts	6	53
Loss carryforward	61	541
Other	25	222
Subtotal	125	1,110
Valuation allowance	(35)	(310)
Total	90	800
Deferred tax liabilities:		
Unrealized gain on available-for-sale securities	(2)	(18)
Total	(2)	(18)
Net deferred tax assets	¥ 88	\$ 782

## 7. FINANCIAL INSTRUMENTS

### a. Overview

(1) Policy for financial instruments

The Company raises funds by borrowing from the parent company and banks. Also, the Company restricts temporary excess fund management to highly secure assets such as time deposits.

(2) Types of financial instruments related risks and risk management

Receivables, such as trade notes and trade accounts, are exposed to the credit risk of customers. In order to mitigate the risk when orders are received, the Company conducts strict screening and determines project plans on the basis of internal guidelines. As investment securities are exposed to market risk, the Company monitors market prices of these securities.

Long-term loans are used for operations or capital investment.

The Company does not engage in derivative transactions.

### b. Fair value of financial instruments

The following table shows the carrying values and fair values of financial instruments as of March 31, 2016, and any differences. Certain financial instruments for which it is extremely difficult to determine the fair value are not included.

At March 31, 2016	Millions of Yen			Thousands of U.S. Dollars		
	Carrying Value	Fair Value	Difference	Carrying Value	Fair Value	Difference
<b>Assets</b>						
Cash and cash equivalents	¥ 399	¥ 399		\$ 3,541	\$ 3,541	
Receivables	4,280	4,280		37,983	37,983	
Investment securities	14	14		124	124	
<b>Liabilities</b>						
Payables	3,377	3,377		29,969	29,969	
Income taxes payable	16	16		142	142	
Advances received on uncompleted construction contracts	1,280	1,280		11,360	11,360	
Long-term loans	69	70	¥ 1	613	621	\$ 8

Note: Current portion of long-term loans is contained in long-term loans

#### Assets

##### Cash and cash equivalents and Receivables

Since cash and cash equivalents and receivables are settled in a short period of time, the carrying value approximates fair value.

##### Investment securities

The fair value of stocks is determined based on quoted market price.

#### Liabilities

##### Payables, Income taxes payable and Advances received on uncompleted construction contracts

Since these accounts are settled in a short period of time, the carrying value approximates fair value.

##### Long-term loans

The fair value is based on the present value of the total principal and interest discounted by an interest rate to be applied if similar new loans are entered into.

*c. Carrying amount of financial instruments whose fair value cannot be reliably determined*

	Millions of Yen	Thousands of U.S. Dollars
	2016	2016
Nonlisted stocks	¥ 44	\$ 391

It is extremely difficult to determine the fair values for these securities since they have no quoted market prices available. Thus, they are not included in "Investment securities" above.

**8. RELATED PARTY DISCLOSURE**

*a. Parent company*

Transactions of the Company with the parent company for the year ended March 31, 2016, were as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2016	2016
Fee for consulting and administrative service	¥ 123	\$ 1,092
Rental fee for land and office buildings	114	1,012
Guarantees of the Company's liabilities	69	612
Guarantees to parent company's liabilities	1,308	11,608
Pledged assets for parent company's liabilities	1,300	11,537

The balances due to or from the parent company at March 31, 2016, were as follows:

	Millions of Yen	Thousands of U.S. Dollars
	2016	2016
Receivables	¥ 842	\$ 7,472
Other assets	59	524
Payables	22	195

Business terms:

1. Fees for consulting and administrative services are decided by negotiation with the parent company based on the amount suggested by the parent company.
2. Rental fee for land and office building is decided by negotiating on an arm's-length basis.
3. The parent company uses a Cash Management System (CMS) for their subsidiaries to control the cash surplus and spend their money efficiently at the group level. The interest rates on loans within the CMS are generally decided based on the current market interest rates available.

Because the loans within the group are made as needed, the amounts of the transactions are omitted in the table above.

***b. Affiliated companies***

Transactions of the Company with affiliated companies for the year ended March 31, 2016, were as follows:

	<u>Millions of Yen</u> <u>2016</u>	<u>Thousands of</u> <u>U.S. Dollars</u> <u>2016</u>
Net sales	¥ 58	\$ 515
Cost of sales	319	2,831
Selling, general and administrative expenses	11	98

The balances due to or from affiliated companies at March 31, 2016, were as follows:

	<u>Millions of Yen</u> <u>2016</u>	<u>Thousands of</u> <u>U.S. Dollars</u> <u>2016</u>
Receivables	¥ 2	\$ 18
Payables	79	701

**9. PER SHARE INFORMATION**

	<u>Millions of Yen</u> <u>2016</u>	<u>U.S. Dollars</u> <u>2016</u>
Per share amounts:		
Net assets	¥ 239.50	\$ 2.13
Basic net income	3.20	0.03

Diluted net income per share is not presented since there are no potentially dilutive shares of common stock issuable upon conversion of the convertible debt.