HAPPINET CORPORATION AND CONSOLIDATED SUBSIDIARIES

Consolidated Financial Statements

March 31, 2005 and 2004

(With Independent Auditors’ Report Thereon)

Note:
The accompanying consolidated financial statements have been compiled from the consolidated financial statements filed with the Ministry of Finance as required by the Securities and Exchange Law of Japan. All figures have been rounded to the nearest million yen.

Happinet Corporation and Consolidated Subsidiaries
Consolidated Balance Sheets
March 31, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars (note 2)
	2005	2004	2005
Assets			
Current assets:			
Cash (note 3)	¥ 8,845	¥ 5,845	$ 82,363
Trade notes and accounts receivable	18,503	18,044	172,297
Inventories	4,430	4,564	41,252
Deferred income taxes (note 7)	863	494	8,036
Other current assets	3,539	3,300	32,955
Less allowance for doubtful receivables	45	243	419
Total current assets	36,135	32,004	336,484
Property, plant and equipment:			
Buildings and structures	898	1,336	8,362
Machinery, equipment and vehicles	872	849	8,120
Tools, furniture and fixtures	465	383	4,330
Land	234	273	2,179
	2,469	2,841	22,991
Less accumulated depreciation	1,267	1,404	11,798
Net property, plant and equipment	1,202	1,437	11,193
Intangible assets, net	637	883	5,931
Investments and other assets:			
Investments in securities (notes 4, 5 and 15)	1,044	1,309	9,722
Refundable deposits	471	462	4,386
Deferred income taxes (note 7)	262	837	2,440
Other investments and other assets	171	190	1,592
Less allowance for doubtful receivables	92	88	857
Total investments and other assets	1,856	2,710	17,283
Total assets	¥ 39,830	¥ 37,034	$ 370,891

	Millions of yen		Thousands of U.S. dollars (note 2)
	2005	2004	2005
Liabilities and Stockholders' Equity			
Current liabilities:			
Trade notes and accounts payable (notes 14 and 15)	¥ 17,628	¥ 16,684	$ 164,149
Other payables (note 14)	1,544	1,424	14,378
Accrued income taxes (note 7)	949	393	8,837
Accrued bonuses	492	332	4,581
Other current liabilities	670	765	6,239
Total current liabilities	21,283	19,598	198,184
Non-current liabilities:			
Liabilities for retirement and severance benefits (note 6)	819	687	7,626
Other non-current liabilities	736	721	6,854
Total non-current liabilities	1,555	1,408	14,480
Total liabilities	22,838	21,006	212,664
Minority interests	–	(29)	–
Stockholders' equity:			
Common stock (note 10):	2,751	2,751	25,617
Authorized 32,000,000 shares; issued and outstanding 12,025,000 shares in 2005 and 2004			
Additional paid-in capital (note 10)	2,776	2,776	25,850
Retained earnings (note 11)	11,263	10,278	104,879
Net unrealized gain on other securities (note 4)	209	257	1,946
Treasury stock	(7)	(5)	(65)
Total stockholders' equity	16,992	16,057	158,227
Commitments and contingencies (note 15)			
Total liabilities and stockholders' equity	¥ 39,830	¥ 37,034	$ 370,891

See accompanying notes to consolidated financial statements.

Happinet Corporation and Consolidated Subsidiaries
Consolidated Statements of Operations
March 31, 2005 and 2004

	Millions of yen				Thousands of U.S. dollars (note 2)	
		2005		2004		2005
Net sales	¥	140,462	¥	122,723	$	1,307,962
Cost of sales (note 14)		123,432		107,997		1,149,381
Gross profit		17,030		14,726		158,581
Selling, general and administrative expenses (notes 8, 9 and 14)		14,063		13,585		130,953
Operating income		2,967		1,141		27,628
Other income (deductions):						
Interest income		0		3		0
Dividend income		11		11		102
Interest expenses		(2)		(0)		(19)
Rent income		19		41		177
Gain on sale of investments in securities (note 4)		21		18		196
Loss on sale/disposal of property, plant and equipment		(88)		(436)		(819)
Loss on devaluation of investments in securities and other investments (note 4)		–		(378)		–
Loss on devaluation of inventories		–		(1,100)		–
Other, net		(7)		(368)		(65)
		(46)		(2,209)		(428)
Income (loss) before income taxes and minority interests		2,921		(1,068)		27,200
Income taxes (note 7):						
Current		1,072		467		9,982
Deferred		239		(848)		2,226
		1,311		(381)		12,208
Income (loss) before minority interests		1,610		(687)		14,992
Minority interests		29		–		270
Net income (loss)	¥	1,581	¥	(687)	$	14,722

	Yen				U.S. dollars (note 2)	
		2005		2004		2005
Per share of common stock (note 1 (m)):						
Net income (loss) – basic	¥	131.53	¥	(57.36)	$	1.22
Cash dividends applicable to the year		22.50		25.00		0.21

See accompanying notes to consolidated financial statements.

Happinet Corporation and Consolidated Subsidiaries
Consolidated Statements of Stockholders' Equity
March 31, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars (note 2)
	2005	2004	2005
Common stock (note 10):			
Balance at beginning of year	¥ 2,751	¥ 2,751	$ 25,617
Balance at end of year	2,751	2,751	25,617
Additional paid-in capital (note 10):			
Balance at beginning of year	2,776	2,776	25,850
Increase resulting from sale of treasury stock	0	0	0
Balance at end of year	2,776	2,776	25,850
Retained earnings (note 11):			
Balance at beginning of year	10,278	11,279	95,707
Decrease resulting from a newly consolidated subsidiary	(326)	(17)	(3,036)
Cash dividends	(270)	(297)	(2,514)
Net income (loss)	1,581	(687)	14,722
Balance at end of year	11,263	10,278	104,879
Net unrealized gain on other securities at end of year (note 4)	209	257	1,946
Treasury stock at end of year	(7)	(5)	(65)
Total stockholders' equity at end of year	¥ 16,992	¥ 16,057	$ 158,227

See accompanying notes to consolidated financial statements.

Happinet Corporation and Consolidated Subsidiaries
Consolidated Statements of Cash Flows
March 31, 2005 and 2004

	Millions of yen		Thousands of U.S. dollars (note 2)
	2005	2004	2005
Cash flows from operating activities:			
Income (loss) before income taxes and minority interests	¥ 2,921	¥ (1,068)	$ 27,200
Adjustments to reconcile income before income taxes and minority interests to net cash provided by (used in) operating activities:			
Depreciation and amortization	516	521	4,805
Allowance for doubtful receivables	(56)	107	(522)
Increase (decrease) in accrued bonuses	159	(16)	1,481
Increase in liabilities for retirement and severance benefits	127	255	1,183
Interest and dividend income	(11)	(14)	(102)
Interest expenses	2	0	19
Loss on sale/disposal of property, plant and equipment	88	436	819
Gain on sale of investments in securities	(21)	(18)	(196)
Loss on devaluation of investments in securities and other investments	–	378	–
Increase in trade notes and accounts receivable	(200)	(654)	(1,862)
Decrease in inventories	408	3,297	3,799
Increase (decrease) in trade notes and accounts payable	646	(3,152)	6,015
Decrease in other payables	(7)	(1)	(65)
Other, net	(801)	(83)	(7,459)
Sub total	3,771	(12)	35,115
Interest and dividend received	11	14	102
Interest paid	(2)	0	(18)
Income taxes paid	(541)	(480)	(5,038)
Net cash provided by (used in) operating activities	3,239	(478)	30,161
Cash flows from investing activities:			
Capital expenditures	(142)	(71)	(1,322)
Proceeds from sale of property, plant and equipment	171	735	1,592
Purchase of intangible assets	(73)	(181)	(680)
Purchase of investments in securities	(69)	(21)	(643)
Proceeds from sale of investments in securities	35	63	326
Other, net	32	(417)	298
Net cash provided by (used in) investing activities	(46)	108	(429)

Cash flows from financing activities:			
(Increase) decrease in treasury stock	(2)	254	(18)
Dividends paid to stockholders	(272)	(299)	(2,533)
Net cash used in financing activities	(274)	(45)	(2,551)
Net increase (decrease) in cash and cash equivalents	2,919	(415)	27,181
Cash and cash equivalents at beginning of year	5,845	6,295	54,428
Cash and cash equivalents of newly consolidated subsidiaries	81	(35)	754
Cash and cash equivalents at end of year (note 3)	¥ 8,845	¥ 5,845	$ 82,363

See accompanying notes to consolidated financial statements.

Happinet Corporation and Consolidated Subsidiaries

Notes to Consolidated Financial Statements

(1) Summary of Significant Accounting Policies

(a) Basis of Presenting Consolidated Financial Statements

Happinet Corporation (the Company) and its consolidated subsidiaries maintain their books of account and prepare their financial statements in conformity with financial accounting standards of Japan.

The accompanying consolidated financial statements have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law and its related accounting regulations, and in conformity with accounting principles and practices generally accepted in Japan, which may differ in some material respects from accounting principles and practices generally accepted in countries and jurisdictions other than Japan.

In preparing the accompanying consolidated financial statements, certain reclassifications have been made in the financial statements issued domestically in Japan in order to present them in a form which is more familiar to readers outside Japan. In addition, the notes to the consolidated financial statements include information which is not required under accounting principles generally accepted in Japan but is presented herein as additional information.

(b) Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries (4 subsidiaries for 2005 and 5 subsidiaries for 2004, respectively).

The Company merged with 3 wholly-owned subsidiaries at April 1, 2005.

All significant intercompany accounts and transactions have been eliminated in consolidation.

Investments in affiliates are accounted for by the equity method.

The Accounting Standards for Consolidation require the control or influence concept for the consolidation scope of subsidiaries and affiliates. Under the control or influence concept, a company in which the parent company or its consolidated subsidiaries, directly or indirectly, are able to exercise control over operations is fully consolidated, and a company over which the parent company and/or its consolidated subsidiaries have the ability to exercise significant influence is accounted for by the equity method.

The excess of cost over the underlying net assets at the dates of investment in subsidiaries is being amortized over 5 years.

(c) Cash and Cash Equivalents

For the purpose of the statements of cash flows, the Company considers all highly liquid investments with insignificant risk of changes in value which have maturities of generally three months or less when purchased to be cash equivalents.

(d) Investments in Securities

Under the Accounting Standards for Financial Instruments, securities are classified into four categories – "trading securities," "held-to-maturity securities," "investments in affiliates" and "other securities." Securities classified as "trading securities" are stated at fair value and unrealized gains or losses are recorded in the consolidated statements of income. Securities classified as "held-to-maturity securities" are stated at amortized cost. Securities classified as "other securities" with fair value are stated at fair value and unrealized gains or losses, net of related taxes, are excluded from earnings and recorded in a separate component of stockholders' equity. Debt classified as "other securities" for which fair value is not available are stated at the amortized cost. Equity securities classified "other securities" for which fair value is not available are stated at the moving-average cost. Realized gains and losses on the other securities are computed using the moving-average cost. Holding securities of the Company are classified as other securities.

(e) Inventories

Inventories are stated at the lower of cost or market. Cost is determined principally by the average method.

(f) Property, Plant and Equipment

Property, plant and equipment are carried substantially at cost. Depreciation is provided by the declining-balance method based on the estimated useful lives, except for the buildings acquired on or after April 1, 1998, which are depreciated based on the straight-line method.

The estimated useful lives are as follows:

Buildings and structures	3 – 47 years
Machinery, equipment and vehicles	3 – 12 years
Tools, furniture and fixtures	2 – 20 years

(g) Intangible Assets

Intangible assets are carried at cost less amortization. Software development expenses are deferred and amortized by the straight-line method over the estimated useful lives (5 years). Intangible assets other than software are deferred and amortized by the straight-line method at rates based on the estimated useful lives of the respective assets.

(h) Allowance for Doubtful Receivables

An allowance for doubtful receivables is provided at an amount of uncollectible receivables based on historical loss ratios and an amount that takes into consideration the possibility of specific liabilities.

(i) Retirement and Severance Benefits

The Company and its consolidated subsidiaries have contributory and noncontributory pension plans to provide retirement and severance benefits to substantially all employees.

Under the Accounting Standards for Retirement and Severance Benefits, provisions have been made in the accompanying consolidated financial statements based on the present value of the projected future retirement and severance benefits attributable to employee services rendered by the end of the year, less amounts funded under pension plans.

In the standards, for smaller-sized companies, the simplified method would be applied to measurement of provisions, and consolidated subsidiaries of the Company had provided the amounts if all eligible employees voluntarily terminated employment at the respective balance sheet date. Effective in the year ended March 31, 2004, consolidated subsidiaries of the Company changed their calculation method of retirement and severance benefits obligation from the simplified method to the principle method. This change was made in order to achieve more appropriate allocation of the subsidiaries' pension cost by adopting the same calculation method of the Company.

Unrecognized transition differences arising from the change at the time the standards introduced which had been amortized over 5 years were fully charged to fiscal 2004 income. Furthermore, unrecognized prior service cost and unrecognized actuarial loss generated in the previous years which had been amortized over 5 years were fully charged to fiscal 2004 income, and the amortization of unrecognized prior service cost and unrecognized actuarial loss are recognized in the year in which they were generated. These changes were made for financial health improvement as a result of reviewing the assumptions of pension plans in consideration of personnel transfers between the Company and its subsidiaries and change in the personnel organization.

Owing to these changes, ¥218 million of unrecognized transition differences, unrecognized prior service cost and unrecognized actuarial loss generated in the previous years were charged to fiscal 2004 income. And ¥38 million of differences between the simplified method and the principle method of the consolidated subsidiaries at April 1, 2003 was charged to fiscal 2004 income.

Due to the changes described above, operating income increased by ¥66 million, and loss before income taxes and minority interests increased by ¥190 million.

(j) Leases

Finance leases, except for those where the legal title of the underlying property is transferred from the lessor to the lessee at the end of the lease term, are accounted for similarly to operating leases.

(k) Income Taxes

The Accounting Standards for Deferred Income Taxes require that deferred income taxes be accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled, and the effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

(l) Appropriation of Retained Earnings

Under the Commercial Code of Japan, the appropriation of retained earnings with respect to a given financial period is made by resolution of the stockholders at a general meeting to be held subsequent to the close of such financial period. The accounts for that period do not, therefore, reflect such appropriation. (See note 11)

(m) Data per Common Share

Net income (loss) per share is computed on the basis of the weighted average number of shares of common stock outstanding during the respective years. (See note 12)

Cash dividends per share are computed based on dividends actually paid during the year. (See note 11)

(n) Reclassifications

Certain reclassifications have been made to the prior years' consolidated financial statements to conform to the presentation used as of and for the year ended March 31, 2005.

(2) Financial Statement Translation

The consolidated financial statements are expressed in Japanese yen. However, solely for the convenience of the reader, the consolidated financial statements as of and for the year ended March 31, 2005 have been translated into United States dollars at the rate of ¥107.39=U.S.$1, the approximate exchange rate on the Tokyo Foreign Exchange Market on March 31, 2005. This translation should not be construed as a representation that the amounts shown could be converted into U.S. dollars at such rate.

(3) Cash and Cash Equivalents

Reconciliation between "Cash" in the accompanying consolidated balance sheets and "Cash and cash equivalents" in the accompanying consolidated statements of cash flows at March 31, 2005 and 2004 is follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Cash	¥ 8,845	¥ 5,845	$ 82,363
Cash and cash equivalents	¥ 8,845	¥ 5,845	$ 82,363

(4) Investments in Securities

Acquisition cost, balance sheet amount and gross unrealized gain and gross unrealized loss of other securities with fair value as of March 31, 2005 and 2004 are summarized as follows:

	Millions of yen			
	Acquisition cost	Gross Unrealized gain	Gross Unrealized loss	Balance sheet amount
March 31, 2005				
Equity securities	¥ 598	¥ 359	¥ (8)	¥ 949
March 31, 2004				
Equity securities	¥ 603	¥ 435	¥ (2)	¥ 1,036

	Thousands of U.S. dollars			
	Acquisition cost	Gross Unrealized gain	Gross Unrealized loss	Balance sheet amount
March 31, 2005				
Equity securities	$ 5,568	$ 3,343	$ (74)	$ 8,837

It is not practicable to estimate the fair value of securities as of March 31, 2005 and 2004 described bellow because of lack of market price and difficulty in estimating fair value.

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Other securities:			
Unlisted equity securities	¥ 74	¥ 19	$ 689

For the years ended March 31, 2005 and 2004, proceeds from sale of other securities are ¥35 million ($326 thousand) and ¥63 million, the gross realized gains are ¥21 million ($196 thousand) and ¥19 million, respectively. The gross realized losses are immaterial for the year ended March 31, 2005, and were ¥1 million for the year ended March 31, 2004.

(5) Investments in Affiliates

The aggregate carrying amounts of investments in affiliates as of March 31, 2005 and 2004 are ¥20 million ($186 thousand) and ¥254 million, respectively.

(6) Retirement and Severance Benefits

The Company and certain consolidated subsidiaries had defined benefit retirement and pension plans, which consist of unfunded retirement and severance plans that provide for lump-sum payment of benefits and contributory benefit plans provided under the Welfare Pension Insurance Law of Japan. The Corporate Defined Benefit Pension Plan Law was enacted, and on January 28, 2005, the Company and certain consolidated subsidiaries obtained the approval from the Minister of Health, Labour and Welfare and dissolved the contributory benefit plans provided under the Welfare Pension Insurance Law of Japan. On April 1, 2005, the Company and certain consolidated subsidiaries introduced a defined contribution retirement and pension plan. Certain consolidated subsidiaries have adopted a defined contribution retirement and pension plan.

The funded status of the pension plans at March 31, 2005 and 2004 is outlined as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Projected benefit obligation	¥ 819	¥ 687	$ 7,626
Amount recognized in the consolidated balance sheets	¥ 819	¥ 687	$ 7,626

Plan assets of the welfare pension fund which are not included in the above table at March 31, 2004 were estimated to be ¥1,669 million.

Net periodic pension cost for the years ended March 31, 2005 and 2004 consists of the following components:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Service cost	¥ 76	¥ 78	$ 708
Interest cost	14	17	130
Differences between the simplified method and the principle method of the consolidated subsidiaries at April 1, 2003	–	38	–
Amortization of prior service cost	–	(34)	–
Amortization of transition obligation existing at April 1, 2000	–	175	–
Amortization of actuarial loss generated in the previous years	–	77	–
Amortization of actuarial loss generated in the current fiscal year	67	26	624
Contribution by the Company to the Welfare Pension Fund	73	83	680
Additional benefits, etc.	1	40	9
Contribution to the defined contribution fund	1	–	9
Net periodic pension cost	¥ 232	¥ 500	$ 2,160

Significant assumptions of pension plans used to determine these amounts in fiscal 2005 and 2004 are as follows:

	2005	2004
Discount rate	1.5%	2.0%
Periodic allocation method for projected benefit	Straight-line	Straight-line
Period for amortization of unrecognized prior service cost	1 year*	1 year*
Period for amortization of unrecognized actuarial loss	1 year*	1 year*
Period for amortization of transition obligation existing at April 1, 2000	–	Fully amortized

Note: *Amortized in the year in which they were generated

(7) Income Taxes

The Company and its consolidated subsidiaries are subject to Japanese corporate, inhabitant and business taxes based on income which, in the aggregate, result in a statutory tax rate of approximately 40.6% in 2005 and 42.0% in 2004.

Amendments to Japanese tax regulations were enacted on March 31, 2003. As a result of these amendments, the normal income tax rate was to be reduced from approximately 42.0% to 40.4% effective from the Company's fiscal year beginning April 1, 2004.

Furthermore, Tokyo Prefectural Government Ordinance was promulgated on October 14, 2003. And, the normal income tax rate was to be changed from approximately 40.4% to 40.6% effective from the Company's fiscal year beginning April 1, 2004. Deferred income tax assets and liabilities as of March 31, 2004 were revaluated at a rate of 40.6%. As a result of the change in the tax rate, net deferred tax assets as of March 31, 2004 were increased by ¥6 million and net unrealized gain on other securities was decreased by ¥1 million, and ¥7 million was credited to income.

A reconciliation of the statutory tax rate and the effective tax rate as a percentage of income (loss) before income taxes and minority interests for the years ended March 31, 2005 and 2004 is follows:

	2005	2004
Statutory tax rate	40.6%	42.0%
Expenses not deductible for tax purposes	0.8	(1.5)
Income not credited for tax purposes	(0.1)	0.2
Per capita tax	0.7	(1.7)
Tax benefits not recognized on operating losses of subsidiaries	1.6	–
Effect of change in the tax rate	–	(3.6)
Other	1.3	0.7
Effective tax rate	44.9%	35.7%

Significant components of deferred tax assets and liabilities at March 31, 2005 and 2004 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Deferred tax assets:			
Deferred tax assets (current):			
Accrued business tax	¥ 73	¥ 27	$ 680
Valuation loss for inventories	462	164	4,302
Accrued bonuses	197	134	1,834
Unrealized profit on sale of inventories eliminated on consolidation	3	–	28
Accrued loss on warehouse etc. closedown	–	33	–
Other	128	136	1,192
	863	494	8,036
Deferred tax assets (non-current):			
Liabilities for retirement and severance benefits	320	263	2,980
Loss on devaluation of other investments	36	44	335
Loss on devaluation of investments in securities	43	51	401
Tax loss carryforwards	–	656	–
Other	32	25	298
Offset with deferred tax liabilities (non-current)	(169)	(202)	(1,574)
	262	837	2,440
Net deferred tax assets	¥ 1,125	¥ 1,331	$ 10,476
Deferred tax liabilities:			
Deferred tax liabilities (non-current):			
Net unrealized gain on other securities	¥ (169)	¥ (176)	$ (1,574)
Gain on evaluation of subsidiaries' assets and liabilities	–	(26)	–
Offset with deferred tax assets (non-current)	169	202	1,574
Net deferred tax liabilities	¥ –	¥ –	$ –

(8) Selling, General and Administrative Expenses

Significant components of selling, general and administrative expenses are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Storage expenses	¥ 1,940	¥ 2,468	$ 18,065
Freight	2,060	2,073	19,182
Promotion	1,078	986	10,038
Salary and executive compensation	4,114	3,631	38,309

(9) Research and Development Costs

Research and development costs charged to income for the years ended March 31, 2005 and 2004 are ¥50 million ($466 thousand) and ¥25 million, respectively.

(10) Common Stock

Under the Commercial Code of Japan, the entire amount of the issue price of shares is required to be designated as stated common stock account although a company in Japan may, by resolution of its Board of Directors, account for an amount not exceeding 50% of the issue price of new shares as additional paid-in capital. On October 1, 2001, the Code was amended to eliminate the provision of common stock par value resulting in all common stock being recorded with no par value.

(11) Retained Earnings and Dividends

The Commercial Code of Japan provides that an amount equal to at least 10% of appropriations paid in cash be appropriated as a legal reserve until an aggregated amount of such reserve and additional paid-in capital equal 25% of common stock. Either additional paid-in capital or the legal reserve may be available for dividends by resolution of the stockholders to the extent that the amount of total additional paid-in capital and legal reserve exceeds 25% of stated common stock. Balances of the legal reserve are included in retained earnings in the accompanying consolidated balance sheets.

The amount available for dividends is based on the amount recorded in the Company's non-consolidated books of account in accordance with the Commercial Code of Japan.

In accordance with the Commercial Code of Japan, proposed appropriations of retained earnings have not been reflected in the financial statements at the end of each fiscal year. The proposed appropriation of retained earnings at March 31, 2005 of cash dividends of ¥12.5 ($0.12) per common share aggregating ¥150 million ($1,397 thousand) and bonuses to directors was approved at the Company’s general meeting of stockholders held on June 17, 2005.

(12) Net Income (Loss) per Share Information

Reconciliation of the numbers and the amounts used in the basic net income (loss) per share computations for the years ended March 31, 2005 and 2004 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Net income (loss) applicable to common stockholders	¥ 1,581	¥ (687)	$ 14,722

	Number of shares (Thousands)	
	2005	2004
Weighted average number of shares on which basic net income (loss) per share is calculated	12,018	11,973

(13) Leases

A summary of assumed amounts of acquisition cost, accumulated depreciation and net book value at March 31, 2005 and 2004 are as follows:

	Millions of yen							
		Machinery, equipment and vehicles		Tools, furniture and fixtures		Intangible assets		Total
March 31, 2005								
Acquisition cost	¥	6	¥	314	¥	340	¥	660
Accumulated depreciation		3		126		290		419
Net book value	¥	3	¥	188	¥	50	¥	241
March 31, 2004								
Acquisition cost	¥	3	¥	305	¥	372	¥	680
Accumulated depreciation		2		221		232		455
Net book value	¥	1	¥	84	¥	140	¥	225

	Thousands of U.S. dollars							
		Machinery, equipment and vehicles		Tools, furniture and fixtures		Intangible assets		Total
March 31, 2005								
Acquisition cost	$	56	$	2,924	$	3,166	$	6,146
Accumulated depreciation		28		1,173		2,701		3,902
Net book value	$	28	$	1,751	$	465	$	2,244

Future minimum payments required under finance leases at March 31, 2005 and 2004 are as follows:

	Millions of yen				Thousands of U.S. dollars	
		2005		2004		2005
Within one year	¥	116	¥	146	$	1,080
Over one year		129		87		1,201
	¥	245	¥	233	$	2,281

Lease payments, depreciation equivalents and amounts representing interest under the finance leases which are accounted for in the same manner as operating leases for the years ended March 31, 2005 and 2004 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Lease payments	¥ 175	¥ 228	$ 1,630
Depreciation equivalents	166	214	1,546
Amounts representing interest	5	10	47

(14) Balances and Transactions with Related Party

The Company's outstanding common stock was owned by Bandai Co., Ltd. by 25% at March 31, 2005 and 2004.

Balances with the company at March 31, 2005 and 2004, and related transactions for the years then ended are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Balances:			
Trade accounts payable	¥ 7,174	¥ 1,412	$ 66,803
Transactions:			
Purchases	¥ 37,482	¥ 5,018	$ 349,027

A director of the Company is concurrently serving as a representative director of IRIMAJIRI SHOUICHIROU, and the balances with the company at March 31, 2005, and related transactions for the year then ended are summarized as follows:

	Millions of yen	Thousands of U.S. dollars
Balances:		
Other payables	¥ –	$ –
Transactions:		
Consultant fee	¥ 6	$ 56

A director of the Company is concurrently serving as a representative director of SENRYAKU KEIEI KAIHATSU Center, and the balances with the company at March 31, 2005 and 2004, and related transactions for the years then ended are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2005	2004	2005
Balances:			
Other payables	¥ 0	¥ 1	$ –
Transactions:			
Consultant fee	¥ 8	¥ 3	$ 74

A corporate auditor of the Company is concurrently serving as a representative of TAKAISHI Law Office, and the balances with the firm at March 31, 2005 and 2004, and related transactions for the years then ended are summarized as follows:

	Millions of yen				Thousands of U.S. dollars	
	2005		2004		2005	
Balances:						
Other payables	¥	–	¥	–	$	–
Transactions:						
Consultant fee	¥	1	¥	2	$	9

Bandai Visual Co., Ltd. is a subsidiary of Bandai Co., Ltd. as at March 31, 2005. Balances with the company at March 31, 2005, and related transactions for the year then ended are summarized as follows:

	Millions of yen		Thousands of U.S. dollars	
Balances:				
Trade accounts payable	¥	487	$	4,535
Transactions:				
Purchases	¥	2,577	$	23,997

(15) Commitments and Contingencies

It is common practice in Japan for companies, in the ordinary course of business, to receive promissory notes in settlement of trade accounts receivable and to subsequently discount such notes at banks or to transfer them by endorsement to suppliers in the settlement of accounts payable. At March 31, 2004, the company was contingently liable with respect to trade notes receivable endorsed in the amounts of ¥12 million.

Investment in securities with a book value of ¥291 million ($2,710 thousand) are pledged for the accounts payable of ¥7 million ($65 thousand) at March 31, 2005.

(16) Segment Information

(a) Industry segments

The Company had categorized its business into the two segments of “Toy and TV game etc. business” and “Video software business.” Effective in the year ended March 31, 2005, the Company changed its management organization reflecting the merger and the business acquisition, and started its new mid to long term management plan. The business segments have been reclassified to reflect these changes more accurately into the five segments as “Toy business”, “Video software business”, “TV game business”, “Amusement business” and “Other business.” The segments are divided based on type of products and natures, sales system and markets.

Segment information by industry for the year ended March 31, 2005 is summarized as follows:

	Millions of yen							
	2005							
	Toy	Video software	TV game	Amusement	Other	Total	Elimination / corporate	Consolidated
Sales to outside customers	¥ 52,067	¥ 45,458	¥ 28,697	¥ 6,319	¥ 7,921	¥ 140,462	¥ –	¥ 140,462
Inter-segment sales	–	–	–	–	–	–	–	–
	52,067	45,458	28,697	6,319	7,921	140,462	–	140,462
Operating expenses	50,331	43,683	28,394	6,186	7,618	136,212	1,283	137,495
Operating income	¥ 1,736	¥ 1,775	¥ 303	¥ 133	¥ 303	¥ 4,250	¥ (1,283)	¥ 2,967
Assets	¥ 10,819	¥ 8,618	¥ 7,459	¥ 1,592	¥ 1,628	¥ 30,116	¥ 9,714	¥ 39,830
Depreciation and amortization	304	64	62	33	35	498	12	510
Capital expenditures	115	47	27	112	21	322	3	325

	Thousands of U.S. dollars							
	2005							
	Toy	Video software	TV game	Amusement	Other	Total	Elimination / corporate	Consolidated
Sales to outside customers	$ 484,840	$ 423,298	$ 267,223	$ 58,841	$ 73,760	$ 1,307,962	$ –	$ 1,307,962
Inter-segment sales	–	–	–	–	–	–	–	–
	484,840	423,298	267,223	28,841	73,760	1,307,962	–	1,307,962
Operating expenses	468,675	406,770	264,401	57,603	70,938	1,268,387	11,947	1,280,334
Operating income	$ 16,165	$ 16,528	$ 2,822	$ 1,238	$ 2,822	$ 39,575	$ (11,947)	$ 27,628
Assets	$ 100,745	$ 80,250	$ 69,457	$ 14,824	$ 15,160	$ 280,436	$ 90,455	$ 370,891
Depreciation and amortization	2,831	596	577	307	326	4,637	112	4,749
Capital expenditures	1,071	438	251	1,043	195	2,998	28	3,026

Notes: 1. The main products of each segment are as follows:

Toy:	Toys for boys and girls.
Video software:	Video software and music software.
TV game:	Game consoles and related software.
Amusement:	Toy vending machines and products sold via the machines.
Other:	Miscellaneous goods and trading cards.

2. The non-categorized operating expenses of ¥1,283 million ($11,947 thousand) for the year ended March 31, 2005 in the Elimination/ corporate line consist primarily of administrative operation expenses.

3. Corporate assets of ¥9,714 million ($90,455 thousand) as of March 31, 2005 in the Elimination/ corporate line consist primarily of cash and deposits, long-term investments (investments in securities) and assets relating to the administrative operations.

Operations by business group for the year ended March 31, 2004 which are restated to conform to the segmentation for the year ended March 31, 2005 are as follows:

	Millions of yen							
	2004							
	Toy	Video software	TV game	Amusement	Other	Total	Elimination / corporate	Consolidated
Sales to outside customers	¥ 53,468	¥ 29,262	¥ 27,185	¥ 5,438	¥ 7,370	¥ 122,723	¥ –	¥ 122,723
Inter-segment sales	–	–	–	–	–	–	–	–
	53,468	29,262	27,185	5,438	7,370	122,723	–	122,723
Operating expenses	53,293	27,912	26,905	5,305	6,995	120,410	1,172	121,582
Operating income	¥ 175	¥ 1,350	¥ 280	¥ 133	¥ 375	¥ 2,313	¥ (1,172)	¥ 1,141
Assets	¥ 13,225	¥ 7,312	¥ 7,741	¥ 1,632	¥ 1,867	¥ 31,777	¥ 5,257	¥ 37,034
Depreciation and amortization	256	26	151	25	29	487	22	509
Capital expenditures	129	69	25	12	3	238	8	246

The following is based on the former business segmentation.

	Millions of yen				
	2004				
	Toy and TV game etc.	Video software	Total	Elimination / corporate	Consolidated
Sales to outside customers	¥ 93,461	¥ 29,262	¥ 122,723	¥ –	¥ 122,723
Inter-segment sales	–	–	–	–	–
	93,461	29,262	122,723	–	122,723
Operating expenses	92,498	27,912	120,410	1,172	121,582
Operating income	¥ 963	¥ 1,350	¥ 2,313	¥ (1,172)	¥ 1,141
Assets	¥ 24,465	¥ 7,312	¥ 31,777	¥ 5,257	¥ 37,034
Depreciation and amortization	461	26	487	22	509
Capital expenditures	169	69	238	8	246

Notes: 1. The main products of each segment are as follows:

Toy and TV game etc.: Toys for boys and girls, Game consoles and related software, Toy vending machines and products sold via the machines, and nursery items.

Video software: Video software and music software.

2. The non-categorized operating expenses ¥1,172 million for the year ended March 31, 2004 in the Elimination/ corporate line consist primarily of administrative operation expenses.

3. Corporate assets ¥5,257 million as of March 31, 2004 in the Elimination/ corporate line consist primarily of cash and deposits, long-term investments (investments in securities) and assets relating to the administrative operations.

4. As described in Note 1 (i), the Company changed its accounting for retirement and severance benefits. As a result of the changes, operating expenses of “Toy and TV game etc.” segment and “Elimination/ corporate” decreased by ¥45 million and ¥27 million, respectively, and operating expenses of “Video software” segment increased by ¥6 million, thereby operating income of “Toy and TV game etc.” segment and “Elimination/ corporate” increased by ¥45 million and ¥27 million, respectively, and operating income of “Video software” segment decreased by ¥6 million.

(b) Geographic segments

Both domestic sales and assets located in Japan are over 90% of all segments for the years ended March 31, 2005 and 2004.

(c) Overseas sales

Overseas sales are less than 10% of consolidated sales for the years ended March 31, 2005 and 2004.

(17) Supplemental Cash Flow Information

Assets and liabilities of the newly consolidated subsidiary in 2004 by acquisition at the inception of consolidation, and net expenditure for acquisition were as follows:

		Millions of yen
Current assets	¥	78
Non-current assets		131
The excess of cost over the underlying net assets		83
Current liabilities		(265)
Non-current liabilities		(56)
Minority interests		29
Acquisition cost of stock		–
Cash and cash equivalents held by acquired subsidiary		12
Net proceeds from acquisition	¥	12

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Independent Auditors' Report

To the Board of Directors of
Happinet Corporation

We have audited the accompanying consolidated balance sheets of Happinet Corporation and consolidated subsidiaries as of March 31, 2005 and 2004, and related consolidated statements of operations, stockholders' equity and cash flows for the years then ended, all expressed in Japanese 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Happinet Corporation and consolidated subsidiaries as of March 31, 2005 and 2004, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in Japan.

As more fully described in Note 16 to the consolidated financial statements, effective in the year ended March 31, 2005, the Company has changed its classification of segmentation in the segment information by industry.

Furthermore, as more fully described in Note 1(i) to the consolidated financial statements, effective in the year ended March 31, 2004, the Company has changed its method of accounting for retirement and severance benefits of consolidated subsidiaries from the simplified method to the principle method. Furthermore, the Company has changed its methods of accounting for unrecognized transition obligation existing at April 1, 2000, unrecognized prior service cost and unrecognized actuarial loss generated in the previous years.

The accompanying consolidated financial statements as of and for the year ended March 31, 2005 have been translated into United States dollars solely for the convenience of the reader. We have recomputed the translation and, in our opinion, the consolidated financial statements expressed in yen have been translated into United States dollars on the basis described in Note 2 to the consolidated financial statements.

Toyo & Co.
Tokyo, Japan
June 17, 2005

Toyo & Co.

See Note 1(a) to the consolidated financial statements which explains the basis of preparing the consolidated financial statements of Happinet Corporation and consolidated subsidiaries under Japanese accounting principles and practices.