

Notes to Consolidated Financial Statements

KONICA CORPORATION AND CONSOLIDATED SUBSIDIARIES

1. Significant Accounting and Reporting Policies

(a) Basis of Presenting Financial Statements

The accompanying consolidated financial statements have been prepared based on the accounts maintained by Konica Corporation (the "Company") and its consolidated subsidiaries in accordance with the provisions set forth in the Japanese Commercial Code (the "Code") and the Securities and Exchange Law and in conformity with accounting principles and practices generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Accounting Standards.

Certain items presented in the consolidated financial statements submitted to the Director of Kanto Finance Bureau in Japan have been reclassified in these accounts for the convenience of readers outside Japan. In addition, the consolidated financial statements of cash flows are not required to be filed with the Ministry of Finance (MOF), but have been prepared and included in the consolidated financial statements.

The consolidated statements of cash flows have been required to be prepared with effect for the year ended March 31, 2000 in accordance with new accounting standards. These new standards specify a format which differs from that used in earlier years, and, accordingly, the comparative periods' consolidated statements of cash flows have been reformatted.

(b) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and, with certain exceptions which are not material, those of its subsidiaries in which it has control. All significant intercompany transactions and accounts and unrealized intercompany profits are eliminated in consolidation.

Investments in unconsolidated subsidiaries and significant affiliates are accounted for by the equity method. Investments in insignificant affiliates are stated at cost.

The excess of cost over the underlying investments in subsidiaries is recognized as goodwill and is amortized on a straight-line basis over a five-year period.

(c) Translation of Foreign Currencies

Translation of Foreign Currency Transactions

Revenue and cost or expense items arising from the transactions of the Company denominated in foreign currencies are translated into Japanese yen at relevant exchange rates prevailing at the time of transactions ("historical rates").

All assets and liabilities denominated in foreign currencies (short-term monetary items) are translated into yen at the historical rates.

Translation of Foreign Currency Financial Statements

The translations of foreign currency financial statements of overseas consolidated subsidiaries and affiliates into Japanese yen are made by applying the exchange rates prevailing at the balance sheet dates for balance sheet items, except that the common stock, additional

paid-in capital and retained earnings accounts are translated at the historical rates and the statements of income and retained earnings are translated at average exchange rates.

(d) Cash and Cash Equivalents

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

(e) Marketable Securities and Investment Securities

Marketable securities and investment securities are stated at cost which is determined by the moving average method.

(f) Inventories

Inventories are valued principally on an average-cost basis.

(g) Property, Plant and Equipment Depreciation

Depreciation of property, plant and equipment for the Company and domestic consolidated subsidiaries is computed using the declining balance method except for depreciation of buildings acquired after April 1, 1998, based on the estimated useful lives of assets which are prescribed by Japanese income tax laws.

Depreciation of buildings acquired after April 1, 1998 is computed using the straight-line method, based on the same estimated useful lives as above. Depreciation of foreign subsidiaries is computed using the straight-line method.

Ordinary maintenance and repairs are charged to income as incurred. Major replacements and improvements are capitalized. When properties are retired or otherwise disposed of, the property and related accumulated depreciation accounts are relieved of the applicable amounts and any differences are charged or credited to income.

(h) Retirement Plans

Employees of the Company are, under normal circumstances, entitled to a lump-sum retirement payment based upon the length of service and current salary at the time of retirement.

The Company has funded pension plans with trust banks and insurance companies to cover a portion of retirement benefits payable to employees. It is the policy of the Company to provide for the "Reserve for employees' retirement allowances" in an amount equivalent to the present value of the liability for such retirement benefits payable to all eligible employees upon their voluntary retirement at the balance sheet dates, less the accumulated balance of fund assets at such dates.

Under the plans, 50 per cent of the retirement benefits payable to employees retiring at their mandatory retirement age is paid out of the pension plans. The past service costs are being amortized over a period of 12 years and 6 months.

Another pension plan provides for a portion of the retirement benefits, the past service cost of which is being amortized over a period of 20 years.

Employees of consolidated domestic subsidiaries are generally covered by unfunded retirement benefit programs. Several of the domestic subsidiaries have funded pension plans to cover a portion of the retirement benefit payments.

(i) Income Taxes

Income taxes of the Company and its domestic subsidiaries consist of corporate income taxes, local inhabitants taxes and enterprise taxes. Deferred income taxes are provided for in respect of temporary differences between the tax basis of assets and liabilities and those as reported in the financial statements. The Company also provides for the anticipated tax effect of future remittances of retained earnings from overseas subsidiaries and affiliated companies.

(j) Research and Development Expenses

Expenses for research and development activities are charged to income as incurred.

(k) Per Share Data

Net income per share of common stock has been computed based on the weighted average number of shares outstanding during the year.

Cash dividends per share shown for each year in the accompanying consolidated statements are dividends declared as applicable to the respective years.

2. United States Dollar Amounts

Amounts in U.S. dollars are included solely for the convenience of readers outside Japan. The rate of ¥106.15=US\$1, the rate of exchange on March 31, 2000, has been used in translation. The inclusion of such amounts is not intended to imply that Japanese yen have been or could be readily converted, realized or settled in U.S. dollars at this rate or any other rate.

3. Cash and Cash Equivalents

Cash and cash equivalents consisted of:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Cash and bank deposits.....	¥53,618	¥40,053	\$505,115
Money management funds	1,404	—	13,227
Cash and cash equivalents	¥55,022	¥40,053	\$518,342

4. Marketable Securities

The aggregate cost and market value of marketable securities included in investment securities as of March 31, 2000 and 1999 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Marketable securities included in current assets:			
Market value	¥19,129	¥17,861	\$180,207
Carrying amount	15,946	16,723	150,221
Unrealized gain	¥ 3,183	¥ 1,138	\$ 29,986
Investment securities:			
Market value	¥26,280	¥26,358	\$247,574
Carrying amount	15,706	13,943	147,960
Unrealized gain	¥10,574	¥12,415	\$ 99,614

Gross unrealized gains and losses pertaining to marketable equity securities as of March 31, 2000 were as follows:

	Millions of yen		Thousands of U.S. dollars	
	Gains	Losses	Gains	Losses
Current.....	¥ 5,961	¥2,660	\$56,156	\$25,059
Non-current.....	10,542	566	99,312	5,332

The net realized gains on marketable equity securities for the fiscal years ended March 31, 2000 and 1999 were ¥172 million (US\$1,620 thousand) and ¥946 million, respectively.

The net valuation loss on marketable equity securities for the fiscal years ended March 31, 2000 and 1999 were ¥1,657 million (US\$15,610 thousand) and ¥269 million, respectively.

5. Investments in and Loans to Unconsolidated Subsidiaries and Affiliates

The following investments in and loans to unconsolidated subsidiaries and affiliates as of March 31, 2000 and 1999 were included in investment securities:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Investments	¥6,298	¥3,205	\$59,331
Loans	335	442	3,156
	¥6,633	¥3,647	\$62,487

A summary of transactions at the balance sheet dates with these unconsolidated subsidiaries and affiliates is as follows:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Sales	¥16,480	¥18,256	\$155,252
Purchases	21,436	21,739	201,941

Transaction balances as of March 31, 2000 and 1999 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Trade receivables.....	¥7,282	¥6,019	\$68,601
Trade payables.....	7,530	6,104	70,937

6. Short-Term & Long-Term Debt

Loans

Short-term and long-term loans as of March 31, 2000 and 1999 are summarized as follows:

	Millions of yen			Thousands of U.S. dollars
	2000	1999		2000
		(Interest rate)		
Short-term loans.....	¥ 94,722	4.51%	¥122,212	\$ 892,341
Current portion of long-term loans	39,985	4.54%	25,822	376,684
Long-term loans	16,907	3.16%	36,594	159,275
	¥151,614		¥184,629	\$1,428,300

The annual maturities of long-term loans as of March 31, 2000 are as follows:

Years ending March 31	Millions of yen		Thousands of U.S. dollars
2002	¥10,195		\$96,043
2003	3,782		35,629
2004	2,286		21,536
2005	526		4,955

Bonds

Bonds as of March 31, 2000 and 1999 are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Bonds	¥60,750	¥57,570	\$572,303

The annual maturity of long-term loans as of March 31, 2000 is as follows:

Years ending March 31	Millions of yen		Thousands of U.S. dollars
2001	¥ 0		\$ 0
2002	15,000		141,309
2003	15,000		141,309
2004	5,000		47,103
2005	5,000		47,103

7. Income Taxes

The statutory tax rates used for calculating deferred tax assets and deferred tax liabilities as of March 31, 2000 and 1999 were 42.1% and 47.7%, respectively. Due to a change in the tax rate during the year ended March 31, 1999, the balances of deferred tax assets and deferred tax liabilities were ¥3,793 million and ¥239 million less, respectively, than they would have been using the tax rate applicable for the year ended March 31, 1998.

At March 31, 2000 and 1999, the reconciliation of the statutory tax rate to the effective income tax rate was as follows:

	2000	1999
Statutory tax rate.....	42.1%	47.7%
Accumulated deficit	9.9	—
Tax effect on loss of a consolidated subsidiary previously not recognized	—	122.7
Valuation allowance.....	—	(16.1)
Effect of tax-rate change	—	(40.8)
Inventories, etc.	—	(35.5)
Other, net	(2.2)	(7.8)
Effective tax rate	39.9	70.2

At March 31, 2000 and 1999, significant components of deferred tax assets and liabilities were as follows:

	Millions of yen	
	2000	1999
Gross deferred tax assets:		
Tax effect on loss of a consolidated subsidiary previously not recognized.....	¥ 2,528	¥12,814
Tax loss carryforward	10,894	7,668
Temporary difference carrying from restructuring	—	1,886
Reserve for employees' retirement allowance....	3,977	3,036
Inventories, etc.	5,015	3,827
Other, net	9,465	5,704
Subtotal	31,879	34,935
Valuation allowance	(4,980)	(6,413)
Deferred tax assets total.....	26,899	28,522
Deferral of taxes on fixed assets.....	(1,619)	(1,798)
Net deferred tax assets.....	¥25,279	¥26,724

8. Research and Development Expenses

Total amounts charged to income for the fiscal years ended March 31, 2000 and 1999 were ¥25,376 million (US\$239,058 thousand) and ¥27,944 million, respectively.

9. Shareholders' Equity

The Japanese Commercial Code provides that an amount equivalent to at least 10 per cent of cash distributions (cash dividends and bonuses to directors and corporate auditors) paid in a fiscal period

should be appropriated to a legal reserve until this reserve equals 25 per cent of stated capital. The legal reserve is not available for cash dividends but may be used to reduce a deficit by a shareholders' resolution or may be capitalized by a Board of Directors' resolution.

On June 29, 2000, the shareholders approved a cash dividend to be paid to shareholders on record as of March 31, 2000 totaling ¥1,788 million (US\$16,844 thousand), at the rate of ¥5.00 (US\$0.05) per share of common stock. The related appropriation of retained earnings to the legal reserve was made in the amount of ¥178 million (US\$1,677 thousand).

10. Commitments and Contingent Liabilities

The Company and its subsidiaries were contingently liable, as of March 31, 2000, for trade notes discounted with banks of ¥89 million (US\$838 thousand) and for loans guaranteed of ¥4,923 million (US\$46,378 thousand).

11. Lease Transactions

Information on the Company's and consolidated subsidiaries' finance lease transactions (except for those which are deemed to transfer the ownership of the leased assets to the lessee) and operating lease transactions are presented below:

Lessee

1. Finance leases

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Machinery & equipment	¥12,154	¥ 6,016	\$114,498
Tools & furniture	4,171	5,747	39,293
Others	647	422	6,095
	16,973	12,185	159,886
Less: Accumulated depreciation	(5,907)	(6,042)	(55,648)
Net book value	¥11,066	¥ 6,143	\$104,249
Depreciation	¥ 2,087	¥ 1,998	\$ 19,661

Depreciation is based on the straight-line method over the lease terms of the lease assets.

The scheduled maturities of future lease rental payments on such lease contracts as of March 31, 2000 and 1999 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Due within one year	¥ 2,869	¥1,844	\$ 27,028
Due over one year	8,196	4,299	77,211
	¥11,066	¥6,143	\$104,239
Lease rental expenses for the year	¥ 2,087	¥1,998	\$ 19,661

2. Operating leases

The scheduled maturities of future lease rental payments on such lease contracts as of March 31, 2000 and 1999 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Due within one year	¥ 5,235	¥ 6,565	\$ 49,317
Due over one year	17,025	22,400	160,386
	¥22,260	¥28,965	\$209,703

Lessor

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Leased tools & furniture:			
Purchase cost	¥1,919	¥1,880	\$18,078
Accumulated depreciation	(1,564)	(1,321)	(14,734)
Net book value	¥ 355	¥ 559	\$ 3,334

The scheduled maturities of future lease rental income on such lease contracts as of March 31, 2000 and 1999 are as follows:

	Millions of yen		Thousands of U.S. dollars
	2000	1999	2000
Due within one year	¥ 300	¥ 367	\$ 2,826
Due over one year	107	276	1,008
	¥ 408	¥ 643	\$ 3,834
Lease rental income for the year	¥1,318	¥1,269	\$12,416
Depreciation for the year	1,146	1,104	10,796

As a result of the amendment to the Consolidated Financial Statement Regulations, the disclosure of information regarding leased assets and finance lease contracts as a lessee/lessor has become mandatory effective from the year ended March 31, 2000.

12. Segment Information

Segment information is reported in accordance with the requirements of the MOF. The photographic materials segment includes photographic film, photographic paper, photofinishing equipment and chemicals, videotapes and others. The business machines segment includes plain-paper copiers, printers, facsimile machines, cameras, optical products and others.