MODEC, INC. and Subsidiaries

Consolidated Financial Statements
As of December 31, 2004 and 2003

MODEC, INC. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

December 31, 2004 and 2003

A S S E T S

	Thousands of Japanese yen		Thousands of U.S. dollars
	2004	2003	2004
CURRENT ASSETS:			
Cash and time deposits	¥14,061,927	¥12,264,061	$134,951
Accounts receivable – trade (Note 16)	14,059,343	15,326,103	134,926
Inventories	165,116	1,924,492	1,585
Short-term loans receivable (Note 16)	9,783,707	8,945,744	93,894
Short-term lease receivable	1,735,858	1,542,278	16,659
Deferred tax assets (Note 11)	451,866	34,922	4,336
Other current assets	2,448,341	2,747,966	23,497
Less- Allowance for bad debts	(5,392)	(3,291)	(52)
Total current assets	42,700,766	42,782,275	409,796
PROPERTY AND EQUIPMENT:			
Buildings and equipment	695,591	702,672	6,675
Vessel (Note 4)	11,744,758	18,160,121	112,714
Less- Accumulated depreciation	(6,731,787)	(14,185,220)	(64,604)
	5,708,562	4,677,573	54,785
INTANGIBLE ASSETS (Note 3)	4,769,788	994,620	45,775
OTHER ASSETS:			
Investment securities (Note 2)	3,882,262	2,492,457	37,258
Long-term loans receivable from an affiliated company (Note 16)	1,745,350	–	16,750
Long-term lease receivable	6,273,428	8,256,419	60,206
Deferred tax assets (Note 11)	1,081,245	701,150	10,377
Other investments	366,038	363,267	3,512
Less- Allowance for bad debts	(6,400)	(5,300)	(61)
	13,341,923	11,807,993	128,042
Total assets	¥66,521,039	¥60,262,461	$638,398

The accompanying notes are an integral part of these balance sheets.

LIABILITIES AND SHAREHOLDERS' EQUITY

	Thousands of Japanese yen		Thousands of U.S. dollars
	2004	2003	2004
CURRENT LIABILITIES:			
Accounts payable - trade	¥10,255,786	¥11,329,727	$98,424
Short-term loans payable (Notes 5 and 6)	12,663,619	8,529,839	121,532
Current portion of long-term loans payable (Note 5)	6,652,649	3,314,132	63,845
Accrued expenses	1,280,488	887,139	12,289
Income taxes payable (Note 11)	1,517,446	313,646	14,563
Provision for product warranty	322,184	24,314	3,092
Deferred tax liabilities (Note 11)	238,298	248,444	2,287
Other current liabilities	1,979,190	1,575,589	18,994
Total current liabilities	34,909,660	26,222,830	335,026
LONG-TERM LIABILITIES:			
Long-term loans payable (Note 5)	6,345,467	13,897,864	60,897
Severance and retirement benefits			
For employees (Note 9)	103,109	95,859	990
For directors and corporate auditors	104,980	50,424	1,007
Deferred tax liabilities (Note 11)	1,378,991	1,676,032	13,234
Other long-term liabilities	–	510,322	–
Total long-term liabilities	7,932,547	16,230,501	76,128
MINORITY INTERESTS IN CONSOLIDATED SUBSIDIARIES	1,393,822	2,627,104	13,376
CONTINGENT LIABILITIES (Note 12)			
SHAREHOLDERS' EQUITY (Note 7):			
Common stock;			
Authorized – 102,868,000 shares			
Issued – 34,008,000 shares and 29,992,000 shares at December 31, 2004 and 2003, respectively	7,159,000	4,659,200	68,704
Capital surplus	7,675,150	5,175,350	73,658
Retained earnings	7,531,745	5,648,661	72,282
Net unrealized holding gains on securities	575,834	337,398	5,526
Foreign currency translation adjustments	(656,489)	(638,583)	(6,300)
Less- Treasury stock at cost	(230)	–	(2)
	22,285,010	15,182,026	213,868
Total liabilities and shareholders' equity	¥66,521,039	¥60,262,461	$638,398

MODEC, INC. and Subsidiaries

CONSOLIDATED STATEMENTS OF INCOME

For the years ended December 31, 2004 and 2003

	Thousands of Japanese yen		Thousands of U.S. dollars
	2004	2003	2004
SALES	¥51,891,763	¥66,751,630	$498,002
COST OF SALES (Note 10)	44,553,251	59,062,170	427,575
Gross profit	7,338,512	7,689,460	70,427
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	3,559,153	3,541,508	34,157
Operating profit	3,779,359	4,147,952	36,270
OTHER INCOME (EXPENSES):			
Interest income and dividend income	842,171	192,944	8,082
Interest expense	(685,374)	(652,810)	(6,577)
Foreign exchange loss, net	(420,480)	(226,608)	(4,036)
Equity in earnings of affiliates	128,327	148,154	1,232
Depreciation of idle assets	(229,126)	(366,598)	(2,199)
Recovery of repair costs	–	369,379	–
Gain from forgiveness of debt	–	361,766	–
Gain from cancellation of derivative transaction	119,056	–	1,143
Loss on sale of property and equipment, net	(44,612)	–	(428)
Loss on bad debt	(242,808)	–	(2,330)
Other, net	167,744	(52,052)	1,609
Total other income (expenses)	(365,102)	(225,825)	(3,504)
INCOME BEFORE INCOME TAXES AND MINORITY INTERESTS	3,414,257	3,922,127	32,766
INCOME TAXES (Note 11):			
Current	2,290,352	1,037,771	21,980
Adjustment to prior years	(489,908)	(191,976)	(4,702)
Deferred	(1,174,044)	197,769	(11,267)
INCOME BEFORE MINORITY INTERESTS	2,787,857	2,878,563	26,755
MINORITY INTERESTS	557,364	849,272	5,349
NET INCOME	¥ 2,230,493	¥ 2,029,291	$ 21,406

	Japanese yen		U.S. dollars
Net income per share (Note 8)	¥72.77	¥72.67	$0.70
Diluted net income per share (Note 8)	—	¥70.54	—
Dividends per share	¥7.50	¥7.50	$0.07

The accompanying notes are an integral part of these statements.

MODEC, INC. and Subsidiaries

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

For the years ended December 31, 2004 and 2003

	Number of shares of common stock	Common stock	Capital surplus	Retained earnings	Net unrealized holding gains on securities	Foreign currency translation adjustments	Treasury stock
		Thousands of Japanese yen					
Balance, December 31, 2002	25,717,000	¥3,133,025	¥2,683,025	¥3,822,247	¥ 33,755	¥ (68,049)	–
Issuance of new shares	4,275,000	1,526,175	2,492,325	–	–	–	–
Net income	–	–	–	2,029,291	–	–	–
Cash dividends paid	–	–	–	(192,877)	–	–	–
Bonuses paid to directors	–	–	–	(10,000)	–	–	–
Change for the year	–	–	–	–	303,643	(570,534)	–
Balance, December 31, 2003	29,992,000	4,659,200	5,175,350	5,648,661	337,398	(638,583)	–
Issuance of new shares	4,016,000	2,499,800	2,499,800	–	–	–	–
Net income	–	–	–	2,230,493	–	–	–
Cash dividends paid	–	–	–	(337,409)	–	–	–
Bonuses paid to directors	–	–	–	(10,000)	–	–	–
Change for the year	–	–	–	–	238,436	(17,906)	–
Purchases of treasury stock	–	–	–	–	–	–	¥(230)
Balance, December 31, 2004	34,008,000	¥7,159,000	¥7,675,150	¥7,531,745	¥575,834	¥(656,489)	¥(230)
		Thousands of U.S. dollars					
Balance, December 31, 2003		$44,714	$49,668	$54,210	$3,238	$(6,128)	–
Issuance of new shares		23,990	23,990	–	–	–	–
Net income		–	–	21,406	–	–	–
Cash dividends paid		–	–	(3,238)	–	–	–
Bonuses paid to directors		–	–	(96)	–	–	–
Change for the year		–	–	–	2,288	(172)	–
Purchases of treasury stock		–	–	–	–	–	$(2)
Balance, December 31, 2004		$68,704	$73,658	$72,282	$5,526	$(6,300)	$(2)

The accompanying notes are an integral part of these statements.

MODEC, INC. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended December 31, 2004 and 2003

	Thousands of Japanese yen		Thousands of U.S. dollars
	2004	2003	2004
CASH FLOWS FROM OPERATING ACTIVITIES:			
Income before income taxes and minority interests	¥ 3,414,257	¥ 3,922,127	$ 32,766
Adjustments to reconcile income before income taxes and minority interests to net cash provided by operating activities:			
Depreciation and amortization	635,640	1,834,224	6,100
Amortization of consolidated differences	26,486	13,243	254
Provision for allowance for bad debts	2,101	7,271	20
Provision for severance and retirement benefits for employees	7,250	11,537	70
Provision for severance and retirement benefits for directors and corporate auditors	54,556	27,981	524
Provision for (reversal of) product warranty	297,870	(23,262)	2,859
Interest income and dividend income	(842,171)	(192,944)	(8,082)
Interest expense	685,374	652,810	6,577
Foreign exchange loss (gain)	96,030	(678,529)	922
Equity in earnings of affiliates	(128,327)	(148,154)	(1,232)
Recovery of repair costs	–	(369,379)	–
Gain from forgiveness of debt	–	(361,766)	–
Gain from cancellation of derivative transaction	(119,056)	–	(1,143)
Loss on sale of property and equipment, net	44,612	–	428
Changes in assets and liabilities:			
Decrease (Increase) in			
– Accounts receivable - trade	3,559,708	(1,255,353)	34,162
– Inventories	1,708,890	9,786,718	16,400
– Consumption taxes refund receivable	46,863	(32,206)	450
Decrease in			
– Accounts payable - trade	(856,050)	(6,345,820)	(8,215)
Bonuses paid to directors	(10,000)	(10,000)	(96)
Other, net	1,002,337	369,617	9,620
	9,626,370	7,208,115	92,384
Interest and dividend received	619,103	152,223	5,941
Interest paid	(426,204)	(681,724)	(4,091)
Recovery of repair costs received	–	286,707	–
Income taxes refund	489,908	–	4,702
Income taxes paid	(685,858)	(1,513,215)	(6,582)
Net cash provided by operating activities	9,623,319	5,452,106	92,354

	Thousands of Japanese yen		Thousands of U.S. dollars
	2004	2003	2004
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchases of property and equipment and intangible assets	¥ (3,785,888)	¥ (301,569)	$ (36,333)
Proceeds from sale of property and equipment and intangible assets	1,486,812	–	14,269
Purchases of investment securities	(100,000)	(149,995)	(960)
Purchases of investments in affiliates	(1,624,995)	(1,290,929)	(15,595)
Disbursement of long-term loans receivable	(27,164,435)	(8,356,919)	(260,695)
Collection of long-term loans receivable	21,785,803	1,890,655	209,077
Purchases of investments in subsidiaries	(4,999,680)	(420,550)	(47,982)
Net cash used in investing activities	(14,402,383)	(8,629,307)	(138,219)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from short-term loans payable	161,116,147	40,545,136	1,546,220
Repayment of short-term loans payable	(156,871,809)	(36,386,302)	(1,505,488)
Proceeds from long-term loans payable	156,300	6,902,207	1,500
Repayment of long-term loans payable	(3,816,005)	(7,545,044)	(36,622)
Issuance of shares	4,999,600	4,018,500	47,981
Cash dividends paid to minority interests	(84,402)	(51,427)	(810)
Cash dividends paid	(334,960)	(192,877)	(3,214)
Other, net	(230)	–	(2)
Net cash provided by financing activities	5,164,641	7,290,193	49,565
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	(119,367)	(84,265)	(1,145)
NET INCREASE IN CASH AND CASH EQUIVALENTS	266,210	4,028,727	2,555
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	13,795,717	6,852,903	132,396
INCREASE IN CASH AND CASH EQUIVALENTS DUE TO ADDITIONAL CONSOLIDATED SUBSIDIARIES	0	2,914,087	0
CASH AND CASH EQUIVALENTS AT ENDING OF YEAR	¥14,061,927	¥13,795,717	$134,951

The accompanying notes are an integral part of these statements.

MODEC, Inc. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Significant Accounting and Reporting Policies

(a) Basis of Presenting Consolidated Financial Statements

The accompanying consolidated financial statements of MODEC, Inc. (the "Company) 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 generally accepted in Japan, which are different in certain respects as to application and disclosure requirements of International Financial Reporting Standards.

The accounts of overseas subsidiaries are based on their accounting records maintained in conformity with generally accepted accounting principles prevailing in the respective countries of domicile. The accompanying consolidated financial statements have been restructured and translated into English (with some expanded descriptions and the inclusion of consolidated statements of shareholders' equity) from the consolidated financial statements of the Company prepared in accordance with Japanese GAAP and filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Securities and Exchange Law. Some supplementary information included in the statutory Japanese language consolidated financial statements, but not required for fair presentation, is not presented in the accompanying consolidated financial statements.

The translation of the Japanese yen amounts into U.S. dollars are included solely for the convenience of readers outside Japan, using the prevailing exchange rate at December 31, 2004, which was ¥104.20 to U.S. $1. The convenience translations should not be construed as representations that the Japanese yen amounts have been, could have been, or could in the future be, converted into U.S. dollars at this or any other rate of exchange.

(b) Principles of Consolidation and Equity Method

The accompanying consolidated financial statements include the accounts of the Company and 15 of its subsidiaries for the year ended December 31, 2004 and 13 of its subsidiaries for the year ended December 31, 2003. Material inter-company balances, transactions and profits have been eliminated in consolidation.

Investments in significant unconsolidated subsidiaries and affiliates, which were 5 companies for the year ended December 31, 2004 and 2003, were accounted for by the equity method.

The consolidated financial statements are required to include the accounts of the Company and significant companies that are controlled by the Company through substantial ownership of more than 50% of the voting rights or through ownership of a high percentage of the voting rights, even if it is equal to or less than 50%, and existence of certain conditions evidencing control by the Company of decision-making bodies of such companies.

Investments in significant unconsolidated subsidiaries and affiliates, of which the Company has ownership of 20% or more but less than or equal to 50%, and of 15% or more and less than 20% and can exercise significant influences over operating financial policies of investees, have been accounted for by the equity method.

All consolidated subsidiaries have the same balance sheet date, December 31, corresponding with that of the Company.

(c) Valuation of Assets and Liabilities of Subsidiaries

In the elimination of investments in subsidiaries, the assets and liabilities of the subsidiaries, including the portion attributable to minority shareholders, were evaluated using the fair value at the time the Company acquired the control of the respective subsidiaries.

(d) Consolidated Differences

The differences between cost and net assets acquired of consolidated subsidiaries and affiliated companies which are accounted for by using the equity method are recognized as consolidated differences and amortized using the straight-line method over estimated useful lives, except that these differences recognized in a consolidated subsidiary in the U.S.A. are treated in accordance with U.S. GAAP.

(e) Securities

In accordance with the Japanese accounting standard for financial instruments, all companies required to examine the intent of holding each security and classify those securities as (a) securities held for trading purposes (hereafter, “trading securities”), (b) debt securities intended to be held to maturity (hereafter, “held-to-maturity debt securities”), (c) equity securities issued by unconsolidated subsidiaries and affiliated companies, and (d) all other securities that are not classified in any of the above categories (hereafter, “available-for-sale securities”).

Based on the examination of the intent of holding, the Company classifies its securities as equity securities issued by unconsolidated subsidiaries and affiliated companies and available-for-sale securities. Available-for-sale securities maturing within one year from the balance sheet date are included in current assets. Other securities are included in investment securities. The Company does not have trading securities or held-to-maturity debt securities.

Equity securities issued by unconsolidated subsidiaries and affiliated companies that are not accounted for by equity method are stated at moving-average cost. Available-for-sale securities with available fair market values are stated at fair market value as of balance sheet dates. Unrealized gains and losses on these securities are reported, net of applicable income taxes, as a separate component of shareholders' equity. Realized gains and losses on sale of such securities are computed using moving-average cost. Available-for-sale securities without available fair market values are stated at moving-average cost.

(f) Inventories

Inventories consist of costs of uncompleted contracts and are stated at cost, determined on an individual project basis.

(g) Property and Equipment

Property and equipment are carried substantially at cost. Depreciation of vessel (Floating Production Storage & Offloading and Floating Storage & Offloading) owned by the consolidated overseas subsidiaries is calculated by using the straight-line method based on their lease term or their economic useful lives.

Depreciation of buildings and equipment is calculated by using the declining-balance method based on their useful lives and residual value prescribed by the Japanese corporation tax laws and regulations, except that buildings, acquired after March 31, 1998, are depreciated using the straight-line method. Consolidated overseas subsidiaries depreciate buildings and equipment using the straight-line method based on their useful lives.

(h) Intangible Assets

The Company amortizes intangible assets using the straight-line method based on their useful lives prescribed by the Japanese corporation tax laws and regulation and amortizes software costs using the straight-line method over the estimated useful life (5 years).

Goodwill of a consolidated overseas subsidiary is amortized using the straight-line method based on the terms of an agreement.

Mining rights of a consolidated overseas subsidiary is amortized using the production method based on the amount of production forecast.

(i) Allowance for Bad Debts

The Company provides a sufficient allowance for bad debts to cover probable losses on collection by estimating uncollectable amounts individually in addition to amounts for possible losses based on actual losses on collection in the past.

(j) Accrued Employees' Bonuses

The Company accrues employees' bonuses based on the estimated amounts to be paid in the subsequent period.

(k) Provision for Product Warranty

Provision for product warranty is provided based on the estimated amounts for covering the probable product warranties.

(l) Severance and Retirement Benefits for Employees

The Company has an unfunded lump-sum severance and retirement payment plan for employees. Under the plan, employees whose employment is terminated or who retire are entitled to benefits which are, in general, determined on the basis of length of service and current basic salary at the time of termination or retirement. If the termination is involuntary, the employees are generally entitled to larger benefits than in the case of voluntary termination or retirement.

The Company provides allowance for employees' severance and retirement benefits based on the estimated amount of projected benefit obligation at the balance sheet date (See Note 9).

(m) Severance and Retirement Benefits for Directors and Corporate Auditors

Subject to shareholders' approval, directors and corporate auditors customarily receive lump-sum payments upon retirement under an unfunded retirement allowances plan.

The Company records severance and retirement benefits for directors and corporate auditors at the amounts payable if all directors and corporate auditors terminated their services at the balance sheet date.

(n) Translation of Foreign Currency Accounts

Foreign currency transactions are translated into Japanese yen using the exchange rate in effect at the time of each transaction or at the applicable exchange rates under forward exchange contracts.

Assets and liabilities denominated in foreign currencies are translated into Japanese yen at the year-end exchange rate, and the resulting gains or losses are included in other income (expenses) in the statements of income.

Financial statements of consolidated overseas subsidiaries are translated into Japanese yen using the exchange rates prevailing at the end of each fiscal year, except the exchange rates in effect at the date of transactions are used for shareholders' equity. The Company records foreign currency translation adjustments in the shareholders' equity.

(o) Finance Lease Transactions without Transfer of Ownership

Finance lease transactions, other than those that transfer ownership of the leased property to the lessee, are accounted for in the same way as operating lease transactions.

(p) Derivative Transactions and Hedge Accounting

Derivative financial instruments of the Company are stated at fair value and gains or losses are recognized as changes in the fair value unless derivative financial instruments are used for hedging purposes.

If derivative financial instruments are used as hedges and meet certain hedging criteria, the Company defers recognition of gains or losses resulting from changes in fair value of derivative financial instruments until the related losses or gains on the hedged items are recognized.

However, in cases where forward foreign exchange contracts are used as hedges and meet certain hedging criteria, forward foreign exchange contracts and hedged items are accounted for in the following manner.

1) If a forward foreign exchange contract is executed to hedge existing foreign currency receivables or payables,
   a) the difference, if any, between the Japanese yen amount of the hedged foreign currency receivable or payable translated using the spot rate at the inception date of the contract and the book value of the receivable or payable is recognized in the income statement in the period which includes the inception date, and
   b) the discount or premium on the contract (that is, the difference between the Japanese yen amount of the contract translated using the contracted forward rate and that translated using the spot rate at the inception date of the contract) is recognized over the term of the contract.

2) If a forward foreign exchange contract is executed to hedge a future transaction denominated in a foreign currency, the future transaction will be recorded using the contracted forward rate, and no gains or losses on the forward foreign exchange contract are recognized.

Also, if interest rate swap contracts are used as hedges and meet certain hedging criteria, the net amount to be paid or received under the interest rate swap contract is added to or deducted from the interest on the assets or liabilities for which the swap contract was executed.

Some consolidated overseas subsidiaries adopt hedge accounting in accordance with U.S. GAAP.

(q) Revenue Recognition

The Company recognizes revenues on contracts by the completed contract method, except for those items whose contract amount is over 1 billion yen and whose term of construction is over one year in which cases the percentage of completion method is used.

The U.S.A. consolidated subsidiary recognizes revenues on all contracts by the percentage of completion method.

(r) Income Taxes

The Company provides income taxes at the amounts currently payable based on taxable income for tax purposes that may be different from income for the accounting purposes. The Company recognizes tax effects of temporary differences between the carrying amounts of assets and liabilities for tax and financial reporting purposes. The asset and liability approach is used to recognize deferred tax assets and liabilities for the expected future tax consequences of the temporary differences.

(s) Cash Flow Statement

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

Reconciliation of cash and time deposits shown in the consolidated balance sheets and cash and cash equivalents in the consolidated statements of cash flows as of December 31, 2004 and 2003 is as follows:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Cash and time deposits	¥14,061,927	¥12,264,061	$134,951
Cash equivalents included in short-term loans receivable	–	1,531,656	–
Cash and cash equivalents	¥14,061,927	¥13,795,717	$134,951

(t) Reclassification

Certain reclassifications have been made to the previously reported fiscal 2003 amounts to conform to fiscal 2004 presentation. These reclassifications had no effect on previously reported net income or total shareholders' equity.

2. Marketable Securities and Investment Securities

(a) The following tables summarize acquisition costs, book values (fair values) of securities with available fair values as of December 31, 2004 and 2003.

	Thousands of Japanese Yen		
2004 :	Acquisition cost	Book value	Difference
Available-for-sale securities:			
Securities with book values exceeding acquisition costs:			
Equity securities	¥310,587	¥1,286,576	¥975,989
Total	¥310,587	¥1,286,576	¥975,989

	Thousands of Japanese Yen		
2003 :	Acquisition cost	Book value	Difference
Available-for-sale securities:			
Securities with book values exceeding acquisition costs:			
Equity securities	¥310,587	¥882,448	¥571,861
Total	¥310,587	¥882,448	¥571,861

2004 :	Thousands of U.S. dollars Acquisition cost	Book value	Difference
Available-for-sale securities:			
Securities with book values exceeding acquisition costs:			
Equity securities	$2,981	$12,347	$9,366
Total	$2,981	$12,347	$9,366

(b) The following table summarizes book values of securities with no available fair values as of December 31, 2004 and 2003.

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Available-for-sale securities:			
Unlisted equity securities	¥ 200,000	¥ 100,000	$ 1,919
Investments in non-consolidated subsidiaries and affiliates:	2,395,685	1,510,008	22,992
Total	¥2,595,685	¥1,610,008	$24,911

3. Consolidated Differences

Consolidated differences included in intangible assets as of December 31, 2004 and 2003 are ¥3,768,431 thousand ($36,165 thousand) and ¥553,152 thousand, respectively.

4. Idle Assets

Book value of fixed assets which are not used by the Company and its consolidated subsidiaries included in vessel as of December 31, 2003 were ¥3,117,100 thousand. There were no idle assets as of December 31, 2004.

5. Loans Payable

Short-term loans payable represent notes payable to banks due generally in twelve months and bearing an average interest rate of 2.1% and 2.2% as of December 31, 2004 and 2003, respectively.

Long-term loans payable as of December 31, 2004 and 2003 are summarized below:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Loans from banks and others, at average rate of 2.3% due through 2009	¥12,998,116	¥17,211,996	$124,742
Less: Current portion included in current liabilities	(6,652,649)	(3,314,132)	(63,845)
	¥6,345,467	¥13,897,864	$60,897

The aggregate annual maturities of long-term loans payable are summarized below:

Year ended December 31,	Thousands of Japanese Yen	Thousands of U.S. dollars
2005	¥ 6,652,649	$ 63,845
2006	1,910,507	18,335
2007	2,009,288	19,283
2008	2,113,071	20,279
2009 and thereafter	312,601	3,000
	¥12,998,116	$124,742

6. Lending Commitment

The Company concluded a commitment line agreement with co-financing consisted of four correspondent financial institutions for the purpose of efficient procurement operating funds. As of December 31, 2004, the commitment line amount is $100,000 thousand, and the amount of loans procured based on the commitment line agreement is $77,000 thousand.

7. Shareholders' Equity

Under the Commercial Code of Japan, the entire amount of the issue price of shares is required to be accounted for as capital, although a company may, by resolution of its Board of Directors, account for an amount not exceeding one-half of the issue price of the new shares as additional paid-in capital, which is included in capital surplus.

The Commercial Code provides that an amount equal to at least 10% of cash dividends and other cash appropriations shall be appropriated and set aside as a legal earnings reserve until the total amount of legal earnings reserve and additional paid-in capital equals 25% of common stock. The legal earnings reserve and additional paid-in capital may be used to eliminate or reduce a deficit by resolution of the shareholders' meeting or may be capitalized by resolution of the Board of Directors. On condition that the total amount of legal earnings reserve and additional paid-in capital remains being equal to or exceeding 25% of common stock, they are available for distribution by the resolution of shareholders' meeting. Legal earnings reserve is included in retained earnings in the accompanying financial statements.

The maximum amount that the Company can distribute as dividends is calculated based on the non-consolidated financial statements of the Company in accordance with the Commercial Code.

The Company issued 2,600,000 and 1,416,000 shares of common stock by the exercise of stock warrants on November 15, 2004 and to the third party on November 24, 2004, respectively. Consequently, common stock increased from ¥4,659,200 thousand to ¥7,159,000 thousand ($68,704 thousand), and additional paid-in capital increased from ¥5,175,350 thousand to ¥7,675,150 thousand ($73,658 thousand).

8. Per Share Data

Net income per share is calculated based on the weighted average number of shares of common stock outstanding during the fiscal year.

Diluted net income per share reflects the effect of potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. There is no outstanding of potential common stock for the year ended December 31, 2004.

9. Severance and Retirement Benefits for Employees

The Company has an unfunded lump-sum severance and retirement payment plan for employees. In accordance with the Japanese accounting standard for employees' severance and pension benefits, a "simpler method" can be adopted to calculate severance and retirement benefits for employees if the number of employees is less than 300. Therefore the Company adopts the "simpler method", and records severance and retirement benefits for employees at the amounts payable if all employees voluntarily terminated their employment at the balance sheet date. None of the consolidated subsidiaries have any termination and retirement allowances plan for employees.

The severance and retirement benefits for employees included in the liability section of the consolidated balance sheets as of December 31, 2004 and 2003 consisted of the following:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Projected benefit obligation	¥103,109	¥95,859	$990
Severance and retirement benefits for employees	¥103,109	¥95,859	$990

Severance and retirement benefit expenses included in the consolidated statements of income for the years ended December 31, 2004 and 2003, are comprised of the following:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Service costs – benefits earned during the year	¥16,109	¥26,816	$155
Severance and retirement benefit expenses	¥16,109	¥26,816	$155

All the severance and retirement benefit expenses are included in "service costs – benefits earned during the year" because the Company adopts the simpler method.

10. Research and Development Costs

Costs relating to research and development activities charged to income for the years ended December 31, 2004 and 2003 are ¥6,828 thousand ($66 thousand) and ¥12,316 thousand, respectively.

11. Income Taxes

The aggregate statutory income tax rate will be reduced for the years commencing on January 1, 2005 or later due to a revised local tax law. At December 31, 2003, the Company applied the reduced aggregate statutory income tax rate of 41% for calculating deferred tax assets and liabilities that are expected to be recovered or settled in the years commencing on January 1, 2005 or later. As a result of this change, net unrealized holding gains on investment securities increased by ¥5,719 thousand, deferred tax liabilities decreased by ¥4,011 thousand and the amount of provision for deferred income taxes increased by ¥1,708 thousand.

The following table summarizes the significant differences between the statutory tax rate and the Company and its consolidated subsidiaries' effective tax rate for financial statement purposes for the years ended December 31, 2004 and 2003:

	2004	2003
Statutory tax rate	42.0%	42.0%
Non-deductible expenses for tax purposes	0.5	0.4
Refund based on tax examination	(15.4)	(3.4)
Taxation on revenue basis of foreign subsidiaries	3.8	4.2
Taxable income excluded from accounting purposes	2.1	–
Deductible expenses excluded from accounting purposes	–	(5.2)
Effect of tax rate change	–	(1.3)
Income of foreign subsidiaries taxed at lower than Japanese normal rate	(10.3)	(6.8)
Tax loss carry forward	2.8	2.7
Equity in earning of affiliates	(1.6)	(1.6)
Realization of tax loss carry forward	(4.8)	–
Credit for foreign taxes	–	(3.1)
Others	(0.8)	(1.2)
Effective tax rate	18.3%	26.7%

Significant components of deferred tax assets and liabilities as of December 31, 2004 and 2003, were as follows:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	20043
Deferred tax assets:			
Current assets:			
Enterprise tax payable	¥105,959	¥27,618	$1,017
Accrued employees' bonuses	18,807	13,442	180
Undistributed profits in a tax haven	31,110	—	299
Credit for foreign taxes	—	32,385	—
Foreign exchange losses	288,444	35,982	2,768
Others	7,546	21,822	72
Sub total	451,866	131,249	4,336
Offset to deferred tax liabilities (short-term)	—	(96,327)	—
Total	451,866	34,922	4,336
Fixed assets:			
Unrealized inter-company profit on fixed assets	954,623	492,009	9,161
Tax loss carry forward	134,482	354,139	1,290

Depreciation	117,766	209,141	1,130
Asset tax in Mexico	—	41,852	—
Severance and retirement benefits for employees	38,541	32,768	370
Others	112,299	45,878	1,079
Sub total	1,357,711	1,175,787	13,030
Valuation allowance	(134,482)	(392,956)	(1,290)
Offset to deferred tax liabilities (long-term)	(141,984)	(81,681)	(1,363)
Total	1,081,245	701,150	10,377
Total deferred tax assets	¥1,533,111	¥736,072	$14,713
Deferred tax liabilities:			
Current liabilities:			
Reduction of tax rate in foreign subsidiaries	¥ (102,045)	¥ (104,105)	$ (979)
Refundable repair costs	(79,033)	(144,339)	(758)
Others	(57,220)	(96,327)	(550)
Sub total	(238,298)	(344,771)	(2,287)
Offset to deferred tax assets (short-term)	—	96,327	—
Total	(238,298)	(248,444)	(2,287)
Long-term liabilities:			
Finance lease	(986,488)	(1,203,821)	(9,467)
Depreciation	(36,150)	(211,953)	(347)
Net unrealized holding gains on securities	(400,156)	(234,463)	(3,840)
Gain from forgiveness of debt	(87,417)	(92,068)	(839)
Others	(10,764)	(15,408)	(104)
Sub total	(1,520,975)	(1,757,713)	(14,597)
Offset to deferred tax assets (long-term)	141,984	81,681	1,363
Total	(1,378,991)	(1,676,032)	(13,234)
Total deferred tax liabilities	(1,617,289)	(1,924,476)	(15,521)
Net deferred tax liabilities	¥(84,178)	¥(1,188,404)	$(808)

12. Contingent Liabilities and Commitments

As of December 31, 2004 and 2003, the Company was contingently liable for the following:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Guarantees of bank loans and other indebtedness for affiliated companies	¥9,745,928	¥5,264,609	$93,531

13. Leases

(a) As Lessee

i) Information on an "as if capitalized" basis of leased property such as acquisition cost, accumulated depreciation, obligations under finance leases and depreciation equivalent of finance leases that do not transfer ownership of the leased property to the lessee for the years ended December 31, 2004 and 2003, are as follows:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
<Buildings and equipment>			
Acquisition cost	¥9,700	¥15,700	$93
Accumulated depreciation	(5,250)	(6,597)	(50)
Net leased property	¥4,450	¥ 9,103	$43

ii) Obligations under finance leases:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Due within one year	¥3,094	¥ 5,083	$30
Due after one year	1,848	4,942	17
Total	¥4,942	¥10,025	$47

iii) Annual lease payments and depreciation equivalent:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Annual lease payments	¥5,084	¥4,830	$49
Depreciation equivalent	4,653	4,430	45
Interest expense equivalent	380	556	4

Depreciation equivalent is computed by a straight-line method over the lease period with no residual value. The difference between total lease payments and acquisition costs under finance leases is recognized as interest expense equivalent, which is allocated to relevant accounting period based on the interest method.

(b) As Lessor

Future lease receivables from operating lease transactions as of December 31, 2004 and 2003, are as follows:

	Thousands of Japanese Yen		Thousands of U.S. dollars
	2004	2003	2004
Due within one year	¥754,408	¥921,444	$7,240
Due after one year	–	–	–
Total	¥754,408	¥921,444	$7,240

14. Derivative Transactions of the Company and its Consolidated Subsidiaries

The Company and its consolidated subsidiaries utilize forward foreign currency contracts in order to hedge currency fluctuation risks arising from export of products in addition to hedging through increases in overseas production and overseas procurement of materials.

The Company and its consolidated subsidiaries also utilize interest rate swaps as derivative transactions in order to hedge interest rate risks of loans payable.

As the derivative transactions are made solely with leading financial institutions, the Company and its consolidated subsidiaries do not expect any credit risks.

The Company follows its internal regulations for derivatives, which stipulate the policy, objective, scope, organization, procedures, and financial institutions to deal with, and has a reporting system for derivative transactions reflecting proper internal control functions.

The following summarizes hedging derivative financial instruments used and items hedged:

Hedging instruments:	Hedged items:
Forward foreign exchange contracts	Foreign currency receivables and payables including future transactions
Currency swap contracts	Foreign currency receivables and payables
Interest rate swap contracts	Foreign currency loans payable

The Company evaluates hedge effectiveness on a semi-annual basis by comparing the cumulative changes in cash flows from or the changes in fair value of hedged items with the corresponding changes in the hedging derivative instruments.

Also, if interest rate swap contracts are used as hedges and meet certain hedging criteria, the net amount to be paid or received under the interest rate swap contract is added to or deducted from the interest on the assets or liabilities for which the swap contract was executed.

Some consolidated overseas subsidiaries adopt hedge accounting in accordance with U.S. GAAP.

The following tables summarize market value information as of December 31, 2004 and 2003 of derivative transactions for which hedge accounting has not been applied:

	Thousands of Japanese Yen			
	Notional amount			
2004:	Total	Due after one year	Market value	Unrealized gain (loss)
Currency related derivatives:				
Forward contracts:				
To sell U.S. dollars	¥320,612	–	¥310,592	¥10,020
				¥10,020

	Thousands of Japanese Yen			
	Notional amount			
2003:	Total	Due after one year	Market value	Unrealized gain (loss)
Currency related derivatives:				
Forward contracts:				
To sell U.S. dollars	¥5,917,624	–	¥5,740,797	¥176,827
				¥176,827

	Thousands of U.S. dollars			
	Notional amount			
2004:	Total	Due after one year	Market value	Unrealized gain (loss)
Currency related derivatives:				
Forward contracts:				
To sell U.S. dollars	$3,077	–	$2,981	$96
				$96

15. Segment Information

Industry segment information for the years ended December 31, 2004 and 2003 is not disclosed because the Company and its consolidated subsidiaries operate a single business relevant to floating production facilities.

Geographical segment information by area for the years ended December 31, 2004 and 2003 is as follows:

	Thousands of Japanese Yen							
2004:	Japan	Asia	Central and South America	North America	Others	Total	Corporate and Elimination	Consolidated
Sales:								
Outside customers	¥18,328,752	¥4,437,888	¥ 2,450,724	¥26,674,399	–	¥51,891,763	–	¥51,891,763
Inter segment	1,108,790	51,991	–	943,855	–	2,104,636	¥ (2,104,636)	–
Total	19,437,542	4,489,879	2,450,724	27,618,254	–	53,996,399	(2,104,636)	51,891,763
Operating expenses	17,943,502	3,263,683	1,200,960	27,798,730	–	50,206,875	(2,094,471)	48,112,404
Operating profit	¥ 1,494,040	¥1,226,196	¥ 1,249,764	¥ (180,476)	–	¥ 3,789,524	¥ (10,165)	¥3,779,359
Assets	¥42,165,399	¥10,179,518	¥12,555,986	¥14,280,875	¥3,781	¥79,185,559	¥(12,664,520)	¥66,521,039

	Thousands of Japanese Yen							
2003:	Japan	Asia	Central and South America	North America	Others	Total	Corporate and Elimination	Consolidated
Sales:								
Outside customers	¥37,973,915	¥4,912,869	¥ 2,731,715	¥21,133,131	–	¥66,751,630	–	¥66,751,630
Inter segment	1,513,265	17,011	–	3,189,017	–	4,719,293	¥ (4,719,293)	–
Total	39,487,180	4,929,880	2,731,715	24,322,148	–	71,470,923	(4,719,293)	66,751,630
Operating expenses	38,356,812	4,393,246	1,188,883	23,782,930	–	67,721,871	(5,118,193)	62,603,678
Operating profit	¥ 1,130,368	¥536,634	¥ 1,542,832	¥ 539,218	–	¥ 3,749,052	¥ 398,900	¥4,147,952
Assets	¥37,286,454	¥8,054,915	¥13,838,357	¥12,236,840	¥5,195	¥71,421,761	¥(11,159,300)	¥60,262,461

	Thousands of U.S. dollars							
2004:	Japan	Asia	Central and South America	North America	Others	Total	Corporate and Elimination	Consolidated
Sales:								
Outside customers	$175,900	$42,590	$ 23,520	$255,992	–	$498,002	–	$498,002
Inter segment	10,641	499	–	9,058	–	20,198	$ (20,198)	–
Total	186,541	43,089	23,520	265,050	–	518,200	(20,198)	498,002
Operating expenses	172,203	31,321	11,526	266,782	–	481,832	(20,100)	461,732
Operating profit	$ 14,338	$11,768	$11,994	$ (1,732)	–	$36,368	$ (98)	$ 36,270
Assets	$404,658	$97,692	$120,499	$137,053	$36	$759,938	$(121,540)	$638,398

The overseas sales of the Company and its consolidated subsidiaries for the years ended December 31, 2004 and 2003 consisted of the following:

	Thousands of Japanese Yen					
2004:	Asia	Africa	Oceania	Central and South America	North America	Total
Overseas sales	¥4,613,475	¥24,202,490	¥17,098,572	¥5,677,457	¥288,294	¥51,880,288
Consolidated sales						¥51,891,763
The ratio of consolidated sales	8.9%	46.6%	33.0%	10.9%	0.6%	100.0%

	Thousands of Japanese Yen					
2003:	Asia	Africa	Oceania	Central and South America	North America	Total
Overseas sales	¥16,742,196	¥21,873,837	¥8,674,662	¥13,546,739	¥5,659,535	¥66,496,969
Consolidated sales						¥66,751,630
The ratio of consolidated sales	25.1%	32.7%	13.0%	20.3%	8.5%	99.6%

	Thousands of U.S. dollars					
2004:	Asia	Africa	Oceania	Central and South America	North America	Total
Overseas net sales	$44,275	$232,270	$164,094	$54,486	$2,766	$497,891
Consolidated sales						$498,002
The ratio of consolidated sales	8.9%	46.6%	33.0%	10.9%	0.6%	100.0%

16. Related Party Transactions

Significant related party transactions and corresponding balances between the Company and unconsolidated subsidiaries and affiliates for the year ended December 31, 2004 and 2003 are as follows:

		Thousands of Japanese Yen		Thousands of U.S. dollars
Related party	Transactions	2004	2003	2004
Buffalo FPSO PTE LTD.	Construction of FPSO	¥1,341,128	−	$12,871
Buffalo FPSO PTE LTD.	Guarantees of bank loans	406,702	¥ 1,446,140	3,903
MODEC FPSO B.V.	Construction of FPSO	25,074	14,975,942	241
MODEC FPSO B.V.	Disbursement of loans receivable	−	9,267,750	−
MODEC FPSO B.V.	Guarantees of bank loans	588,779	−	5,650
MODEC VENTURE 10 B.V.	Construction of FPSO	−	2,018,032	−
MODEC VENTURE 10 B.V.	Guarantees of bank loans	8,750,446	3,818,470	83,977
MODEC VENTURE 11 B.V.	Construction of FPSO	15,311,351	6,044,398	146,942
IMC-MODEC JV 1 PTE LTD.	Disbursement of loans receivable	771,705	−	7,406

		Thousands of Japanese Yen		Thousands of U.S. dollars
Related party	Balances	2004	2003	2004
Buffalo FPSO PTE LTD.	Accounts receivable - trade	¥1,292,080	−	$12,400
MODEC FPSO B.V.	Accounts receivable - trade	3,070,588	¥3,157,224	29,468
MODEC FPSO B.V.	Short-term loans receivable	−	7,414,088	−
MODEC FPSO B.V.	Long-term loans receivable	1,745,350	−	16,750
MODEC VENTURE 10 B.V.	Accounts receivable - trade	−	380,933	−
MODEC VENTURE 10 B.V.	Short-term loans receivable	3,344,539	−	32,097
MODEC VENTURE 11 B.V.	Accounts receivable - trade	2,516,529	6,044,398	24,151
MODEC VENTURE 11 B.V.	Short-term loans receivable	6,097,784	−	58,520
IMC-MODEC JV 1 PTE LTD.	Short-term loans receivable	771,705	−	7,406