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Matters for Online Disclosure under the Law and  
Articles of Incorporation

## **Notes to the Consolidated Financial Statements**

### **Notes to the Non-Consolidated Financial Statements**

27th Term (April 1, 2016 – March 31, 2017)

Sosei Group Corporation

The Notes to the Consolidated Financial Statements and Notes to the Non-Consolidated Financial Statements are provided to shareholders through inclusion on the Company's Internet website (<http://www.sosei.com/>) in accordance with the law and the provisions of Article 14 of the Articles of Incorporation.

## Notes to the Consolidated Financial Statements

### 1. Notes on significant matters that serve as the basis for preparation of the consolidated financial statements

#### (1) Standards for preparation of the consolidated financial statements

The consolidated financial statements have been prepared in conformance with International Financial Reporting Standards (hereinafter "IFRS") based on Paragraph 1, Article 120 of the Corporate Accounting Rules. Some statements and notes required by IFRS have been omitted pursuant to the provisions of the latter part of the Paragraph.

#### (2) Matters related to the scope of consolidation

##### 1) Consolidated subsidiaries

i. Number of subsidiaries: 7

ii. Names of principal consolidated subsidiaries

Sosei Co., Ltd.

Sosei R&D Ltd.

Activus Pharma Co., Ltd.

Heptares Therapeutics Ltd.

iii. Changes in the scope of consolidation

JITSUBO Co., Ltd., which was a consolidated subsidiary in the previous fiscal year, is removed from the scope of consolidation from the fiscal year under review since the Company's ownership ratio decreased due to the third-party allocation of shares.

#### (3) Matters related to application of the equity method

##### 1) Non-consolidated subsidiaries and affiliates accounted for by the equity method

i. Number of non-consolidated subsidiaries and affiliates accounted for by the equity method:

1

ii. Names of principal companies

JITSUBO Co., Ltd.

iii. Changes in the scope of application of the equity method

JITSUBO Co., Ltd., which was a consolidated subsidiary in the previous fiscal year, is included in affiliates accounted for by the equity method from the fiscal year under review since the Company's ownership ratio decreased due to the third party allocation of shares.

#### (4) Matters related to the fiscal year, etc. of consolidated subsidiaries

The settlement date of Sosei RMF1 Limited Partnership for Investment is December 31. Upon preparing the consolidated financial statements, financial statements based on the provisional settlement of accounts as of the consolidated settlement date are used. The settlement date of other consolidated subsidiaries coincides with the end of consolidated fiscal year.

#### (5) Matters related to accounting policies

##### 1) Valuation standards and methods for significant assets

i. Valuation standards and methods for financial assets

• Derivatives

Derivatives are initially recognized at fair value on the date the contract is concluded and recalculated at fair value after initial recognition.

- Non-derivatives

Recognition and measurement of financial instruments

“Trade and other receivables” are recognized on the date of occurrence and other financial assets are recognized on the transaction date on which the Company becomes a contractual party of the financial instrument, and are initially measured at fair value plus transactions costs.

Financial liabilities are recognized on the date on which the Company becomes a contractual party of the financial instrument, and are measured at fair value net of transaction costs.

Derecognition of financial instruments

When contractual rights on cash flow from financial instruments expire, or when contractual rights to receive cash flow from financial instruments are transferred by the Group through a transaction in which all risk and economic value attending ownership of the financial instrument are effectively transferred, recognition of financial instruments is cancelled.

Recognition of financial instruments is cancelled when contractual obligations are exempted or cancelled or when they expire.

The Group categorizes financial instruments as follows.

Available-for-sale financial assets: Non-derivate financial assets designated as available-for-sale financial assets or which are not categorized in any of the categories below. These assets are initially measured at face value at the time of recognition and then re-measured at fair value at the end of each fiscal period. Changes in fair value are recognized as other comprehensive income. When asset recognition is cancelled, the cumulative total recognized in equity as other comprehensive income is reclassified into financial income or financial expenses.

Receivables: Non-derivative financial assets in which the payment amount is fixed or can be fixed and which do not have a public value on an active market. These assets are initially measured at fair value at the time of recognition, and measured with depreciation using the effective interest method at the end of each fiscal period after deducting impairment loss. “Trade and other receivables” is in this category.

Financial liabilities measured with depreciation: Non-derivative financial obligations. These liabilities are initially measured at fair value at the time of recognition, and are measured with depreciation using the effective interest method at the end of each fiscal period. “Trade and other payables” and “Interest-bearing liabilities” are in this category.

Financial liabilities measured with fair value through net profit or loss: Contingent consideration and appraisal value of repayment obligations to the limited partners of a subsidiary, RMF1 Limited Partnership for Investment (hereinafter “RMF1”). These liabilities are initially measured at fair value at the time of recognition and realized or unrealized profit or loss arising from the changes in fair value is recognized as net profit or loss at the time it is generated. “Conditional prices for business combinations” and “Other financial liabilities” are in this category.

- Impairment loss on financial assets

Regarding financial assets measured with depreciation, evaluations are conducted on whether objective evidence exists showing that impairment has occurred at each

reporting date. Regarding financial assets, assets are judged as impaired when objective evidence shows that impairment has occurred after initial recognition of the asset and when that impairment loss can be rationally predicted to negatively impact estimated future cash flow of the financial asset.

Objective evidence showing that financial assets measured with depreciation are impaired includes non-performance of payment or default by an obligor, extension of the collection deadline on receivables conducted under terms that would not likely be applied if the situation had not occurred, signs of bankruptcy of the obligor or issuing company, the disappearance of an active market, etc.

The Group considers evidence of impairment of financial assets measured with depreciation for each individual asset and overall. Regarding significant individual financial assets, impairment is assessed individually. Regarding significant individual financial assets for which separate impairment is not necessary, whether impairment has occurred but has not yet been reported is assessed on an overall basis. Individual financial assets that are not significant are grouped on the basis of similarity of risk characteristics and impairment is assessed overall.

When assessing impairment on an overall basis, Group management judges the possibility that the actual loss is too high or too low based on past trends and depending on current economic and credit conditions, after considering past trends related to default potential, recovery timing and amount of loss occurring, and makes adjustments.

Regarding impairment loss on financial assets measured with depreciation, it is measured as the difference between the book value and the current value of estimated future cash flow net of the asset's initial effective interest, and recognized in net income/loss through the allowance for doubtful accounts. The allowance for doubtful accounts related to financial assets measured with depreciation is directly impaired when future recovery cannot be realistically expected and all collateral is realized or transferred to the Group.

When an event where impairment loss is reduced after impairment loss has been recognized occurs, the decrease in impairment loss (decrease to the allowance for doubtful accounts) is reversed in net income/loss. Regarding impairment loss, it is reversed up to an amount not exceeding depreciation at the time impairment loss was reversed in the case impairment loss was not recognized.

ii. Valuation standards and methods for non-financial assets

• Property, plant and equipment

Property, plant and equipment is measured using the cost model at the acquisition cost net of cumulative depreciation and cumulative impairment. The acquisition cost includes costs directly related to acquiring the asset and the initial estimate of costs for dismantling and removal and restoration of the installation location to its original state.

• Goodwill and intangible assets

Goodwill

Goodwill that occurs when a subsidiary is acquired is stated in "Goodwill" using the acquisition cost net of cumulative impairment. Regarding measurement of goodwill at the time of initial recognition, it is measured using the fair value of transfer considerations, including the amount recognized for non-controlling interests, net of the net recognized

value (normally, the fair value) of identifiable assets and assumed liabilities at the time of the acquisition.

Goodwill is not amortized; it is allocated to cash-generating units identified based on the region where business is conducted and type of business, and an impairment test is conducted each term, or each time there are signs of impairment.

#### Intangible assets

Intangible assets are measured using the cost model; individually acquired intangible assets with estimated service lives that can be defined are measured at the acquisition cost net of cumulative amortization and cumulative impairment. The acquisition cost includes costs directly related to acquiring the asset.

#### Development assets

Outlays for research activities are recognized as costs in the period they occurred.

Internally generated intangible assets that occur at the development stage are recognized only when all of the following can be substantiated.

- Technical feasibility of completing an intangible asset that can be used or sold
- Intention to complete the intangible asset and then use it or sell it
- Ability to use or sell the intangible asset
- Method by which the intangible asset will create future economic benefit with strong potential
- Possibility of using financial or other resources that will be necessary to complete the intangible asset and use it or sell it
- Ability to reliably measure outlays caused by the intangible asset during its period of development

The amount initially recognized for internally generated intangible assets is the total of costs that occurred from the date that the intangible asset initially met the above recognition standards. When an internally generated intangible asset cannot be recognized, development outlays are expensed in the period they occur.

Internally generated intangible assets after initial recognition are stated, just as with other intangible assets, at the acquisition cost net of cumulative amortization and cumulative impairment.

Intangible assets acquired through business combinations and recognized separately from goodwill are stated at the acquisition cost net of cumulative amortization and cumulative impairment after the initial recognition at fair value as of the acquisition date in a policy similar to that applicable to intangible assets acquired independently.

#### Impairment of non-financial assets

Regarding the book values of the Group's non-financial assets, the existence of any signs of impairment is judged on each reporting date. If signs of impairment exist, the asset's recoverable value is estimated. For goodwill and intangible assets with indeterminate service lives or that cannot yet be used, the recoverable value is estimated in a given period in each consolidated fiscal year.

The recoverable value of assets or cash-generating units is the value in use or fair value net of disposition costs, whichever is higher. In the calculation of value in use,

estimated future cash flow is discounted to present value using a pre-tax discount rate that reflects the time value of money and risks inherent to the asset. Regarding cash-generating units, assets groups are the smallest unit generating cash flow that is basically independent from the cash inflows of other assets or asset groups as a result of continued use.

Regarding cash-generating units for goodwill, goodwill is determined based on units managed for the purposes of internal reporting, but, in principle, each company is a cash-generating unit.

Corporate assets do not generate independent cash inflow, so when there are signs of impairment in corporate assets, the recoverable value of the cash-generating unit to which the corporate asset belongs is calculated and the determination made.

Impairment loss is recognized in net income/loss when the book value of the asset or cash-generating unit exceeds the recoverable value. Impairment loss recognized in connection with cash-generating units is first allocated so that the book value of goodwill allocated to that cash-generating unit decreases, and is next allocated so that the book values of other assets within the cash-generating unit decrease proportionally.

Regarding impairment loss related to goodwill, reversal is not conducted. Regarding impairment loss on other assets recognized in the past, the existence of signs showing that the loss has decreased or been eliminated is determined on each reporting date. If there are signs of impairment reversal and the estimate used for determining recoverable value has changed, impairment loss is reversed.

Impairment loss is reversed up to an amount not exceeding the book value after deducting necessary depreciation or amortization costs from it in the case impairment loss was not recognized.

## 2) Depreciation methods for significant depreciable assets

### i. Property, plant and equipment

Depreciation is calculated by calculating depreciable value using the straight-line method over the estimated service life of each component.

Estimated service lives used in calculating depreciation are as follows.

Buildings and structures: 3-15 years

Machinery and equipment: 5-8 years

Tools, furniture and fixtures: 3-10 years

When asset depreciation methods, estimated service lives and residual values are reviewed at the end of each fiscal year and there are changes, they are applied toward the future as changes in accounting estimates.

### ii. Intangible assets

For amortization, the amortizable amount is calculated using the straight-line method over the estimated service lives of constitutive elements. Asset amortization methods, estimated service lives and residual values are reviewed at the end of each fiscal year, and when there changes, they are applied toward the future as changes in accounting estimates.

The main estimated service lives used in calculating amortization are as follows.

Base technology: 20 years

Customer-related assets: 20 years

Intangible assets with indefinite service lives and intangible assets that are not yet usable are not amortized; impairment tests are conducted during a certain period each year and when there are signs of impairment.

iii. Leases (Lessee)

Leases in which nearly all the risk and reward of ownership are transferred to the Group are categorized as finance leases. Finance leases are stated as assets at the fair value of the lease property calculated when the lease began or the present value of minimum lease payments, whichever is lower, and depreciated over the lease period or service life, whichever is shorter. Lease obligations are recognized as interest-bearing liabilities. The portion of lease payments corresponding to finance charges is recognized as an expense over the lease period using the effective interest method.

Lease agreements other than finance leases are categorized as operating leases. Operating lease payments are recognized as expenses on a straight-line basis over the lease period.

3) Accounting standards for significant income and expenses

The Group calculates income based on the fair value of having been received or receivable income.

i. Sales of goods

Income from sales of goods is recognized when the significant risks and rewards of ownership of the goods are transferred to the customer, there is no ongoing managerial commitment to the goods, an inflow of economic benefit related to the transaction is probable, and cost and income amounts occurring related to the transaction can be reliability measured.

The timing of the transfer of risks and rewards of goods ownership differs depending on the individual sales contract, but normally income is recognized when the goods are transferred to the customer or on the shipping date, etc.

ii. Royalty revenue, milestone revenue and lump-sum payments

Royalty revenue that is income received as a fixed rate of sales after the product is marketed, is stated in accordance with the terms of license agreements.

Lump-sum payments that is income received when licensing agreements are concluded and milestone income that is income received based on the progress of research and development (when a development stage is reached that has been stipulated in advance in the agreement) are received from third parties. Such income is normally stated with achievement of the milestone agreed to by both parties.

4) Standards for conversion of significant foreign-denominated assets and liabilities to Japanese currency

i. Foreign-denominated transactions

Foreign-denominated transactions are converted to the functional currencies of Group companies at prevailing exchange rates on the transaction date. Foreign-denominated monetary assets and liabilities on the term-end date are reconverted to the functional

currency at the exchange rate on the term-end date. Foreign-denominated monetary assets and liabilities measured at fair value are reconverted to the functional currency at the exchange rate on the date fair value is calculated. Non-monetary items measured based on acquisition cost are calculated using the exchange rate on the transaction date.

Exchange differences resulting from reversion or settlement are recognized in net income/loss for that period.

ii. Financial statements of foreign operations

The assets and liabilities of foreign operations (overseas subsidiaries, etc.) are converted to Japanese yen at the exchange rate on the term-end date, and their income and expenses are converted to Japanese yen at the average exchange rate.

Foreign exchange differences resulting from conversion of the financial statements of foreign operations are recognized in "Other comprehensive income", and the cumulative difference is stated in "Other components of equity" on the consolidated statement of financial position.

5) Business combinations

Business combinations are accounted for using the acquisition method. Acquisition considerations are measured as the total of assets transferred and liabilities assumed in exchange for control of the acquired business and the fair value on the transaction date of equity instruments issued by the Company. If the acquisition value exceeds the fair value of identifiable assets and liabilities, it is stated as goodwill on the consolidated statement financial position. Conversely, if less, it is directly stated as income in the consolidated statement of comprehensive income. If initial accounting for a business combination is not completed by the end of the term in which the business combination occurred, accounting is conducted with provisional amounts, and the provisional amounts are revised in the measurement period within one year of the acquisition date. Acquisition costs that occurred are accounted for as expenses.

**2. Notes on consolidated statement of financial position**

(1) Cumulative depreciation on property, plant and equipment: 553 million yen

**3. Notes on the consolidated statement of changes in equity**

(1) Matters related to total shares outstanding

Share class	Shares at beginning of consolidated fiscal year	Increase in shares during consolidated fiscal year	Decrease in shares during consolidated fiscal year	Shares at end of consolidated fiscal year
Common shares	16,855,284	60,900	—	16,916,184

Note: The increase in total shares outstanding is due to issuing 60,900 shares through the exercise of stock options.

(2) Matters related to subscription warrants, etc. at the end of the consolidated fiscal year under review

Type and number of shares for subscription warrants at the end of the consolidated fiscal year under review (excluding warrants prior to the first day of their exercise period):  
Common shares 65,200



#### 4. Notes on financial instruments

##### (1) Matters related to financial instruments

###### 1) Policies for management of financial instruments

The Group limits its investments to short-term instruments with minimal risk and does not engage in speculative transactions. Also, funds are primarily procured by issuing new stock and borrowing from banks, etc.

###### 2) Financial instrument content and their risks, and risk management framework

Trade and other receivables are exposed to customer credit risk. Regarding this risk, deadlines and balances are managed for each transaction partner. Trade and other payables have payment deadlines of within one year.

The Group limits its investments to short-term deposits, etc. to reduce risk.

##### (2) Matters related to the fair value, etc. of financial instruments

Amounts stated on the consolidated statement of financial position, fair values and their differences on March 31, 2017 are as follows.

Type	Amount stated on consolidated statement of financial position (JPY Million)*	Fair value (JPY Million)	Difference (JPY Million)
Cash and cash equivalents	13,899	13,899	—
Trade and other receivables	1,382	1,382	—
Trade and other payables	△1,547	△1,547	—
Interest-bearing liabilities	△6,900	△6,900	—
Contingent consideration related to corporate acquisition	△5,230	△5,230	—
Other financial liabilities	△625	△625	—

\*Items stated as liabilities are marked as negative (△).

Notes: Matters related to calculation methods for the market values of financial instruments

1. Cash and cash equivalents, trade and other receivables, and trade and other payables  
These are settled over short time periods, so market values are nearly equivalent to book values and so accord with book values.

###### 2. Interest-bearing liabilities

Borrowings are valued using the amortized cost method, and book values are reasonable approximations of fair values.

###### 3. Interest-bearing liabilities scheduled for repayment after the consolidated settlement date

(JPY Million)

	Within 1 year	Within 1-5years

Interest-bearing liabilities (including long-term)	△1,990	△4,910
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4. Contingent consideration related to corporate acquisition

Such considerations are calculated by discounting by a fixed discount rate upon taking into account conditions such as the probability of occurrence in future cash flow.

5. Other financial liabilities

Other financial liabilities are valued according to the fluctuation in the fair value of the asset of the Company's subsidiary, RMF1.

**5. Notes on per-share information**

(1) Equity attributable to owners of parent company per share	¥1,704.94
(2) Basic net income per share	¥579.97

**6. Notes on important subsequent events**

(1) Important share purchase

MiNA Holdings Limited

(a) Summary of business combination

The Company made investment for a 25.6% equity share of a private UK biopharmaceutical company and pioneer in RNA activation therapeutics (small activating RNAs, saRNAs) through Sosei R&D.

(b) Purpose of purchase

The agreement is consistent with the Company's stated inorganic growth strategy, which is focused on identifying innovative clinical-stage assets that have the potential to be developed rapidly and in addition could be commercialized by the Company in select markets. This inorganic strategy is complementary to the Company's organic strategy, which is focused on advancing a growing pipeline of novel pre-clinical and clinical drug candidates originating from Heptares Therapeutics, a subsidiary of the Company.

(c) Summary of MiNA

Company name	MiNA Holdings Limited
Address	96 Kensington High Street, London, W8 4SG, United Kingdom
Representative's name and title	Robert Habib, CEO
Business description	Pioneering novel treatments harnessing gene activation mechanisms through small activating RNA (saRNA)
Founded	2008

(d) The date of share purchase

2 May, 2017

(e) Method of purchase

Cash in compensation for the shares

(f) Amount of purchase

¥5,057 million

Note: A payment agreement on contingent consideration is included and necessary adjustments to consideration for the acquisition may be carried out. At this point, we do not identify the amount of assets and liabilities of MiNA that the Group will acquire.

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## Notes to the Non-Consolidated Financial Statements

### 1. Notes on matters related to significant accounting policies

- (1) Asset valuation standards and methods
  - 1) Marketable securities
    - A. Subsidiary stock: At cost determined by the moving-average method
- (2) Fixed asset depreciation methods
  - 1) Property, plant and equipment: The declining balance method is used. However, the straight-line method is used for facilities attached to buildings and structures acquired on or after April 1, 2016. The main service lives are as follows.  
Buildings (facilities attached to buildings): 15 years  
Tools, furniture and fixtures: 4-20 years
  - 2) Intangible fixed assets  
The straight-line method is used.  
For internal-use software, the straight-line method is used based on the estimated useful life (5 years) internally.
- (3) Accounting for deferred assets  
Stock issuance expenses    Expensed in full at the time of payment.
- (4) Recognition standards for allowances
  - 1) Allowance for doubtful accounts  
To provide for credit loss on accounts receivable and other accounts, an estimated unrecoverable amount is set aside based on historical credit loss rates for ordinary receivables and based on individual considerations for receivables specified as doubtful, etc.
  - 2) Allowance for bonuses  
To provide for the payment of employee bonuses, of the total estimated amount, the amount estimated to be incurred as an expense that fiscal year is set aside.
- (5) Standards for conversion of significant foreign-denominated assets and liabilities to Japanese currency  
Foreign-denominated monetary claims and obligations are converted to Japanese yen based on spot exchange rates on the term-end date, and translation differences are accounted for as income/loss.
- (6) Other matters that serve as the basis for preparation of the financial statements  
Accounting for consumption taxes, etc.  
Consumption taxes, etc. are accounted for using the tax-exclusion method.

**2. Notes on changes in accounting policies**

(Application of Practical Solution on a Change in Depreciation Method due to Tax Reform 2016)

In accordance with the amendment of the Corporation Tax Act, the Company applied "Practical Solution on a Change in Depreciation Method due to Tax Reform 2016" (Practical Issues Task Force (PITF) No. 32, June 17, 2016) from the fiscal year under review and has changed the method of depreciation for facilities attached to buildings and structures acquired on or after April 1, 2016 from the declining balance method to the straight line method.

The effect of this change on non-consolidated financial statements for the fiscal year under review is immaterial.

### 3. Notes on changes in presentation method

“Accounts receivable from affiliated companies,” which was included in “Other” current assets until the previous fiscal year (¥353 million in the previous fiscal year), is presented separately since it increased monetary importance.

### 4. Notes on the balance sheet (JPY Million)

(1) Cumulative depreciation on property, plant and equipment	16
(2) Monetary claims and obligations to subsidiaries and affiliates (excluding presented items)	
Monetary obligations to subsidiaries and affiliates	144

### 5. Notes on the income statement (JPY Million)

Transactions with subsidiaries and affiliates	
Operating transactions	1,499
Non-operating transactions	2,332

### 6. Notes on the statement of changes in shareholders' equity

No treasury stock is held.

### 7. Notes on tax effect accounting

(1) Main causes for the occurrence of deferred tax assets	(JPY Million)
Deferred tax assets	
Tax loss carryforward	499
Stock in subsidiaries and affiliates	3,324
Other	346
Deferred tax assets subtotal	4,169
Valuation allowance	-4,169
Total deferred tax assets	-

## 8. Notes on transactions with related parties

### (1) Subsidiaries, etc.

Type	Name of company, etc.	Share of voting rights holding (held) (%)	Relationship with related parties	Transaction content	Transaction amount (JPY million)	Account	Ending balance (JPY Million)
Subsidiary	Sosei Co., Ltd.	Direct holding 100.0	Contracted for management operations	Operational contracts	12	Long-term receivable-subsidaries and affiliates	535
				Financial support	Loans of funds Recovery of funds	545 345	Long-term loans to subsidiaries and affiliates
Subsidiary	Activus Pharma Co., Ltd.	Direct holding 100.0	Financial support	Loans of funds Recovery of funds	840 590	Long-term loans to subsidiaries and affiliates	940
Subsidiary	Sosei R&D Ltd.	Direct holding 100.0	Contracted for management operations	Operational contracts	166	Accounts receivable-subsidaries and affiliates	44
Subsidiary	Heptares Therapeutics Ltd.	Direct holding 100.0	Contracted for management operations	Operational contracts	1,313	Accounts receivable-subsidaries and affiliates	1,373
				Reimbursement of cost	Advance payment of contingent consideration	5,146	Accounts payable to subsidiaries and affiliates
Affiliate	JITSUBO Co., Ltd.	Direct holding 43.5	Underwriting of capital increase	Underwriting of capital increase	1,000	—	—

Notes:

- Transaction amounts do not include consumption taxes, etc.; term-end balances include consumption taxes, etc.

2. Prices and other transaction terms are determined upon discussion and agreement by the two parties premised on terms equivalent to other parties unrelated to the Company.
3. Loans of funds to Sosei Co., Ltd. and Activus Pharma Co., Ltd. are determined upon considering market interest rates. Collateral is not received.
4. An allowance for doubtful accounts of ¥955 Million has been set aside for doubtful subsidiary accounts.

(2) Officers and major individual shareholders, etc.

Type	Name	Share of voting rights holding (held) (%)		Relationship with related parties	Transaction content	Transaction amount (JPY million)	Account	Ending balance (JPY Million)
Officer	Malcolm Weir	Directly held	0	Executive Officer and Vice President	Payment of contingent consideration	218	-	-
Officer	Fiona Marshall	Directly held	0	Executive Officer and Vice President	Payment of contingent consideration	159	-	-

Note:

1. The price and other transaction conditions are determined based on the contract contents similar to those used for third parties unrelated to the Company.

**9. Notes on per-share information**

(1) Net assets per share	¥2,414.01
(2) Net income per share	¥59.45