

## News & Information

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**Subsidiary Tracking Stock**  
**Sony Communication Network Corporation**  
**Consolidated Financial Results for the**  
**Fiscal year ended March 31, 2004**



Sony Communication Network Corporation (hereinafter, the "SCN"), a subsidiary the performance of which is linked to a tracking stock issued by Sony Corporation, announced today its consolidated results for the year ended March 31, 2004 (the period from April 1, 2003 to March 31, 2004).

These results are based on the generally accepted accounting standards of Japan.

- **For FY2003 results, although there was an increase in broadband subscribers, there was an intensification of competition for subscribers. As a result, there was an operating loss.**  
During the year ended March 31, 2004, sales decreased 1.6%, compared with the year ended March 31, 2003, to 38,166 million yen. An operating loss of 870 million yen and an ordinary loss of 911 million yen were recorded. Net loss for the year under review was 412 million yen.
- **So-net subscribers total 2.3 million, including 550,000 broadband subscribers.**  
The SCN maintained the level of 2.3 million subscribers reached at the end of the previous fiscal year. The number of broadband subscribers, mainly of ADSL, reached 550,000, an increase by 31% over the end of the previous fiscal year.
- **Fiscal Year 2004 Forecast: expected turn towards profitability due to an expected increase in sales of Internet-related services and expected cost reductions.**  
Regarding the Forecast of Consolidated Results for the year ending March 31, 2005, sales are expected to reach 40,000 million yen, an increase of 4.8%, as a result of a rise in revenue per subscriber due to an increase in the proportion of broadband subscribers, especially of FTTH subscribers, and an increase in Internet-related services. In terms of profitability, with judicious management of customer acquisition costs (such as marketing and sales promotion expenses) and reductions, begun in the prior year, of communication line expenses through integration of access points, it is expected that operating income of 100 million yen, ordinary income of 100 million yen, and net income of 50 million yen will be recorded. Furthermore, at the end of the year ending March 31, 2005, it is estimated that the number of So-net subscribers will reach 2.35 million, of which the SCN aims for over 700,000 to be broadband subscribers.

### Consolidated Results for the year ended March 31, 2004

(Millions of Yen)

	Year ended March 31		Change (%)
	2003	2004	
Sales	38,795	38,166	(1.6)
Operating income (loss)	472	(870)	—
Ordinary income (loss)	96	(911)	—
Net income (loss)	(16)	(412)	—

## **[Operating Results and Financial Condition]**

### **a. Operating Results**

#### **Summary of Consolidated Operations**

During the year under review, the Japanese economy showed signs of moderate economic growth. Factors in the economic background included a correction in the strength of the yen, an improvement in corporate profitability, and an improving trend in individual consumption.

Under these economic conditions, in the Internet sector, the number of Internet users in Japan was over 36 million as of March 2004, an increase of about 6 million from the year earlier period. Within that total, as the transition from narrowband to broadband continued, the number of broadband users passed 14 million users (including ADSL, FTTH, and CATV), an increase of about 4.7 million. (Data according to the Ministry of Public Management, Home Affairs, Posts and Telecommunications.)

In this business environment, the SCN, in addition to strengthening its broadband connection services and broadband content services, began offering a portal service for televisions.

Furthermore, in order to acquire new subscribers, the SCN aggressively implemented new subscriber promotions in cooperation with carriers, such as a campaign offering three months of free broadband. As a result, the SCN was able to maintain the March 2003 level of 2.3 million subscribers, and within that, the number of broadband subscribers reached 550,000 (including users of such services as “Flets” which is operated by regional NTT East and NTT West Corporations).

Under these circumstances, sales for the SCN for the year ended March 31, 2004 decreased 1.6% to 38,166 million yen, compared with sales of 38,795 million yen in the year ended March 31, 2003. Although there was a sales increase related to a rise in broadband subscribers, and an increase in the sales of subsidiaries, there were negative impacts from a decrease in narrowband subscribers and free-promotion campaigns.

Regarding profitability, despite lower costs for communication lines as a result of access point integration, reduced expenses for outsourcing thanks to efficiency improvements at call centers, and improvements in profitability at consolidated subsidiaries, there were increases in costs related to the creation of broadband content and increased expenses for subscriber acquisition, such as sales promotion campaigns. As a result, an operating loss of 870 million yen was recorded, compared with operating income of 472 million yen in the prior fiscal year.

Furthermore, equity losses of 30 million yen, compared with 437 million yen in the prior year, were recorded due to affiliated companies accounted for by the equity method—Label Gate Co., Ltd. and DeNA Co., Ltd. As a result, an ordinary loss of 911 million yen was recorded, compared with ordinary income of 96 million yen in the prior fiscal year.

Under extraordinary gain, gain on issuance of stock by equity investee of 613 million yen and gain on sale of investment in affiliate of 81 million yen were recorded. However, under extraordinary loss, write-off of goodwill of 84 million yen, loss on revaluation of investments in other securities of 90 million yen, and loss on impairment of long-lived assets relating to decided withdrawal from certain operations of 87 million yen were recorded.

An income tax current expense of 16 million yen and income tax deferred benefit of 163 million yen were recorded. As a result, net loss during the year under review was 412 million yen, compared with a net loss of 16 million yen in the prior fiscal year.

## Sales by Category

Year ended March 31, 2004

		Year ended March 31, 2003 (millions of yen)	Percentage of total (%)	<b>Year ended March 31, 2004 (millions of yen)</b>	Percentage of total (%)	Year-on- year change (%)
Operating revenue	Internet provider services	32,245	83.1	<b>30,731</b>	80.5	(4.7)
	Internet- related services	5,161	13.3	<b>6,523</b>	17.1	26.4
Merchandise sales		1,389	3.6	<b>912</b>	2.4	(34.3)
Total		38,795	100.0	<b>38,166</b>	100.0	(1.6)

The three-months ended March 31, 2004

		Three-months ended March 31, 2003 (millions of yen)	Percentage of total (%)	<b>Three-months ended March 31, 2004 (millions of yen)</b>	Percentage of total (%)	Year-on- year change (%)
Operating revenue	Internet provider services	7,762	81.8	<b>7,491</b>	78.3	(3.5)
	Internet- related services	1,355	14.3	<b>1,812</b>	19.0	33.8
Merchandise sales		371	3.9	<b>260</b>	2.7	(30.0)
Total		9,488	100.0	<b>9,562</b>	100.0	0.8

### «Operating revenue»

#### ISP services

In this category, the SCN has focused on broadband and worked to enrich its areas of service, including ADSL and FTTH offerings as well as newly established services such as wireless. Also, in the areas of high-value added connection services, the SCN has started an FTTH service that offers an IP telephone service, So-net Phone.

- Connection Services
  - FTTH (expanded cooperation with carriers)
    - So-net Hikari (Chubu Electric) access “commuf@” service started
    - UCOM home service started
    - “B Flets” Family Pack started
    - So-net Hikari (TEPCO (Tokyo Electric)) apartment service established
  - ADSL (high-speed/area expansion)
    - 1M, 40M courses started
    - 156GC starts operation in FY03. (total 873GC)
  - Mobile Wireless LAN (service start)
    - MVNO bitwarp PDA course started
- Valued-added Connection Services
  - So-net Phone (for B Flets, TEPCO, UCOM)

As a result, sales of ISP services for the year ended March 31, 2004 were 30,731 million yen, a decrease of 4.7% compared with the prior fiscal year. Such sales accounted for 80.5% of total sales, a decrease of 2.6 points. This reflected the free sales promotion campaigns throughout the year, although there was a rise in revenue per subscriber thanks to an increase in the proportion of broadband subscribers.

#### Internet-related services

In this category, the SCN worked to efficiently manage its content offerings through careful selection of businesses, while continuing to actively develop and introduce broadband contents.

- Broadband contents
  - Launch of online jukebox “Wonder Juke” and “Wonder Juke Classic”
  - Korean dramas “Truth” and “Secret” (Internet and CS broadcasting)
- Start of service for television
  - Offering of portal services for Plasma Wega and AirBoard
- Encourage more intense usage by diversification of payment methods for subscription content
  - eMoney “Edy” settlement
  - Safe and simple settlement by “eLIO” credit card

Sales of consolidated subsidiaries (excluding sales related to Merchandise sales) increased and as a result, sales in this category during the year under review increased 26.4% to 6,523 million yen. Sales in this category accounted for 17.1% of total sales, an increase of 3.8 points.

#### **<<Merchandise sales>>**

In this category, sales for the year ended March 31, 2004 were 912 million yen, a decrease of 34.3% compared with the prior fiscal year. Such sales accounted for 2.4% of total sales, a decrease of 1.2 points. The decrease was a result of the decline of sales of the broadband unit for PlayStation 2, which had strong sales during the prior year, as well as of the Sony-made broadband AV Router “HN-RT1” and “PostPet v.3” software.

### **Results of Consolidated Subsidiaries and of Affiliated Companies Accounted for by the Equity Method**

The SCN includes the following four consolidated subsidiaries: So-net Sports.com Corp., So-net M3 Inc., So-net M3 U.S.A. Corp.(hereinafter “M3 U.S.A.”), and Skygate, Co., Ltd. Affiliated companies accounted for by the equity method include Label Gate Co., Ltd. and DeNA Co., Ltd. During the year under review, equity losses were held to 30 million yen, compared to 437 million during the prior fiscal year, due to continued profitability throughout the year at DeNA Co., Ltd.

Of these, M3 U.S.A. was established in November and began marketing activities for the purpose of beginning services of its “MR-kun” site in the United States.

On the other hand, So-net Sports.com Corp. and Skygate, Co., Ltd. saw satisfactory performance in some areas, but from a profitability standpoint, harsh conditions continued.

Furthermore, liquidation of Drivegate Inc., which had operated used-car related sites, was completed in March 2004.

## **b. Analysis of Financial Conditions**

### **Assets, Liabilities, Capital Accounts**

At the end of the year ended March 31, 2004, assets were 13,001 million yen, a decrease of 1,050 million yen from the end of the year ended March 31, 2003. This was primarily due to a decrease of 1,230 million yen in current assets.

The decrease in current assets was mainly due decreases in the combined amounts of deposits in Sony group company and cash and bank deposits of 1,202 million yen and a decrease in inventories of 149 million yen. Non-current assets increased 180 million yen. This increase was mainly a result of an increase in long-term loans, software, and recognition of deferred tax assets related to net operating losses, offset somewhat by a decrease in amortization of goodwill and loss on impairment of certain investments in others.

On the other hand, at the end of the year ended March 31, 2004, liabilities had decreased by 668 million yen compared with the end of the year ended March 31, 2003. This resulted from a decrease in current liabilities of 713 million yen and an increase in long-term liabilities of 45 million yen. The main factor in the decrease in current liabilities was a repayment of long-term debt of 800 million yen to Sony Corp.

Total stockholders' equity decreased by 408 million yen. This was due to a recording of net loss of 412 million yen during the year under review.

### **Cash Flow**

Cash and cash equivalents were 2,182 million yen at the end of the year ended March 31, 2004, a decrease of 1,202 million yen from the end of the prior fiscal year. During the year under review, the SCN generated 129 million yen of cash in operating activities, used 529 million yen of cash in investing activities, and used 800 million yen of cash in financing activities.

#### **<Cash flows from operating activities>**

During the year ended March 31, 2004, regarding cash flows from operating activities, the SCN generated 129 million yen, largely worse than during the year ended March 31, 2003 when the SCN generated 2,077 million yen. This was mainly due to an increase in net loss before income taxes from 269 million yen in the prior fiscal year to 534 million yen in the year under review; an increase in accounts payable, trade of 36 million yen during the year under review, compared with 460 million yen in the prior fiscal year; and a decrease in accrued expenses of 199 million yen compared with an increase of 176 million yen during the prior fiscal year. Also, net loss before income taxes during the year under review included gain on issuance of stock by equity investee of 613 million yen as a non-cash earning, compared with none the prior fiscal year, and equity in net losses of affiliated companies of 30 million yen as a non-cash charge, compared with 437 million yen in the prior fiscal year.

#### **<Cash flows from investing activities>**

During the year ended March 31, 2004, regarding cash flows from investing activities, the SCN used only 529 million yen, while during the year ended March 31, 2003, the SCN used 1,993 million yen. Factors influencing a decrease in net cash out flows from investing activities of the year under review compared with those of the prior fiscal year included a reduction in payment for securities investment in from 1,134 million yen in the prior fiscal year to 122 million yen during the year under review. Also, outlays for acquisition of intangible assets such as connection services and e-commerce related systems were 971 million yen, compared with outlays of 620 million yen in the prior fiscal year, and proceeds from repayment of loans to affiliated companies were 749 million yen

during the year under review.

<Cash flows from financing activities>

During the year ended March 31, 2004, regarding cash flows from financing activities, the SCN used 800 million yen, while during the year ended March 31, 2003, the SCN used 1,340 million yen. During the year under review, this reflected the repayment of long-term debt to Sony Corp.

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## Condensed Consolidated Statements of Income

For the year ended March 31, 2004

(Millions of yen)

	Year ended March 31		Change
	2003	2004	
Sales	38,795	<b>38,166</b>	(1.6%)
Cost of sales	22,725	<b>23,569</b>	
Gross profit	16,070	<b>14,598</b>	
Selling, general and administrative expenses	15,598	<b>15,468</b>	
Operating income (loss)	472	<b>(870)</b>	—%
Non-operating income	117	<b>261</b>	
Non-operating expenses			
Equity in net loss of affiliated companies	437	<b>30</b>	
Other	57	<b>271</b>	<b>302</b>
Ordinary income (loss)	96	<b>(911)</b>	—%
Extraordinary gain			
Gain on issuance of stock by equity investee	0	<b>613</b>	
Gain on sale of investment in affiliate	—	<b>81</b>	<b>695</b>
Extraordinary loss			
Loss on revaluation of investments in other securities	251	<b>90</b>	
Loss on issuance of stock by equity investee	—	<b>1</b>	
Loss on withdrawal from certain operations	—	<b>56</b>	
Loss on impairment of long-lived assets	—	<b>87</b>	
Write off of goodwill	—	<b>84</b>	
Loss from lease cancellation due to service integration and re-examination	114	—	<b>318</b>
Net income (loss) before income taxes	(269)	<b>(534)</b>	—%
Income tax current	128	<b>16</b>	
Income tax deferred	(332)	<b>(163)</b>	<b>(147)</b>
Minority interests in loss (earnings) of consolidated subsidiaries	49	<b>(25)</b>	
Net income (loss)	(16)	<b>(412)</b>	—%

**For the three-months ended March 31, 2004****(Millions of Yen)**

	<b>Three-months ended March 31</b>			<b>Change</b>
	<b>2003</b>	<b>2004</b>		
Sales		9,488	<b>9,562</b>	0.8%
Cost of sales		5,730	<b>5,763</b>	
Gross profit		3,758	<b>3,799</b>	
Selling, general and administrative expenses		4,259	<b>3,743</b>	
Operating income (loss)		(501)	<b>56</b>	—%
Non-operating income		55	<b>53</b>	
Non-operating expenses				
Equity in net loss of affiliated companies	163		<b>26</b>	
Other	(9)	154	<b>77</b>	<b>103</b>
Ordinary income (loss)		(599)	<b>6</b>	—%
Extraordinary loss				
Loss on issuance of stock by equity investee	—		<b>0</b>	
Loss on revaluation of investments in other securities	251		<b>62</b>	
Loss on withdrawal from certain operations	—		<b>2</b>	
Loss on impairment of long-lived assets	—		<b>87</b>	
Write off of goodwill	—		<b>84</b>	
Loss from lease cancellation due to service integration and re-examination	114	365	—	<b>235</b>
Net income (loss) before income taxes		(964)	<b>(229)</b>	—%
Income tax current	(341)		<b>(70)</b>	
Income tax deferred	(310)	(651)	<b>(15)</b>	<b>(85)</b>
Minority interests in loss (earnings) of consolidated subsidiaries		21	<b>(5)</b>	
Net income (loss)		(293)	<b>(320)</b>	—%

## Condensed Consolidated Balance Sheets

(Millions of yen)

	March 31 2003	March 31 2004	Change
<b>ASSETS</b>			
Current assets	<u>8,594</u>	<u>7,363</u>	<u>(1,230)</u>
Cash and bank deposit	517	840	324
Notes and account receivable, trade	3,803	3,891	89
Inventories	278	130	(149)
Deposits in Sony group company	2,867	1,342	(1,526)
Deferred tax assets	472	356	(117)
Other	704	828	124
Allowance for bad debt	(47)	(23)	24
Non-current assets	<u>5,458</u>	<u>5,637</u>	<u>180</u>
Property, plant and equipment	<u>349</u>	<u>256</u>	<u>(92)</u>
Furniture and fixtures	232	162	(71)
Other	116	94	(22)
Intangible assets	<u>2,465</u>	<u>2,263</u>	<u>(202)</u>
Software	1,141	1,286	145
Goodwill	1,104	708	(395)
Other	220	269	49
Investment and other assets	<u>2,644</u>	<u>3,118</u>	<u>474</u>
Investments in affiliates and others	1,618	1,495	(123)
Deferred tax assets	498	773	275
Other	527	849	322
Total assets	<u>14,051</u>	<u>13,001</u>	<u>(1,050)</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
Current liabilities	<u>5,880</u>	<u>5,167</u>	<u>(713)</u>
Account payable, trade	2,428	2,463	36
Current portion of long-term borrowing from parent Company	800	—	(800)
Accrued expense	1,889	1,711	(179)
Accrued income taxes	127	197	71
Accrued bonuses	217	239	22
Accrued customer incentive program	—	81	81
Other	419	475	56
Long-term liabilities	<u>94</u>	<u>140</u>	<u>45</u>
Accrued severance costs for employees	65	93	28
Accrued severance indemnities for directors	29	47	17
Total liabilities	<u>5,974</u>	<u>5,306</u>	<u>(668)</u>
Minority interest	<u>33</u>	<u>58</u>	<u>25</u>
Common stock	5,246	5,246	—
Additional paid-in capital	4,765	4,765	—
Retained earnings (accumulated losses)	(1,961)	(2,373)	(412)
Unrealized exchange losses of investment securities	(6)	—	6
Foreign currency translation adjustments	—	(1)	(1)
Total stockholders' equity	<u>8,044</u>	<u>7,636</u>	<u>(408)</u>
Total liabilities and stockholders' equity	<u>14,051</u>	<u>13,001</u>	<u>(1,050)</u>

## Consolidated Statements of Additional Paid-in Capital and Retained Earnings and Accumulated Losses

(millions of yen)

Item	Year ended March 31, 2003	Year ended March 31, 2004
Additional Paid-in Capital		
Balance at the beginning of the year	4,765	4,765
Balance at the end of the year	4,765	4,765
Retained Earnings (Accumulated Losses)		
Balance at the beginning of the year	(1,945)	(1,961)
Increase		
Net loss	16	412
Balance at the end of the year	(1,961)	(2,373)

## Consolidated Statements of Cash Flow

For the year ended March 31, 2004

(Millions of yen)

	<b>Year ended March 31</b>	
	<u>2003</u>	<u>2004</u>
I. Cash flows from operating activities		
Net income(loss) before income taxes	(269)	(534)
Depreciation and amortization	773	836
Loss on impairment of long-lived assets	—	87
Amortization for goodwill	311	311
Write-off of goodwill	—	84
Gain on issuances of stock by equity investee	(0)	(613)
Loss on issuance of stock by equity investee	—	1
Equity in net loss of affiliated companies	437	30
Loss on revaluation of investments in other securities	251	90
Gain on sale of investments in affiliate	—	(81)
Loss on withdrawal from certain operations	—	56
Increase (decrease) in accrued bonuses	(25)	22
Increase in accrued severance costs for employees	23	28
Increase in accrued severance indemnities for directors	13	17
Increase (decrease) in allowance for bad debt	19	(24)
Increase in accrued customer incentive program	—	81
Interest and dividend income	(8)	(9)
Interest expenses	7	3
Loss on disposal of tangible fixed assets	47	93
Loss on sales of tangible fixed assets	—	10
Gain on sales of tangible fixed assets	—	(1)
(Increase) decrease in account receivable, trade	184	(89)
(Increase) decrease in inventories	(214)	149
Increase in other current assets	(141)	(136)
Increase in accounts payable, trade	460	36
Increase (decrease) in accrued expenses	176	(199)
Increase in other current liabilities	161	61
Sub Total	<u>2,207</u>	<u>309</u>
Receipt of interest and dividends	8	9
Payments for interest	(7)	(3)
Payments for income taxes	(131)	(186)
Net cash provided by operating activities	<u>2,077</u>	<u>129</u>

	<b>(Millions of yen)</b>	
	<b>Year ended March 31</b>	
	<b>2003</b>	<b>2004</b>
II. Cash flows from investing activities		
Payment for securities investment	(1,134)	(122)
Proceeds from sales of securities investment	—	231
Payment for acquisition of fixed assets	(51)	(37)
Proceeds from sales of fixed assets	7	4
Payment for acquisition of intangible assets	(620)	(971)
Proceeds from sales of intangible assets	20	0
Payment for deposits	(43)	(4)
Proceeds from deposits	101	1
Payments for long-term prepaid expenses	(32)	(203)
Net cash increase resulting from acquiring subsidiary	30	—
Payments for loan	(271)	(178)
Repayment of loan	—	749
Net cash used in investing activities	<u>(1,993)</u>	<u>(529)</u>
III. Cash flows from financing activities		
Decrease in short-term borrowing	(140)	—
Payments of long-term debt	(1,200)	(800)
Net cash used in financing activities	<u>(1,340)</u>	<u>(800)</u>
IV. Effect of exchange rate difference on cash and cash equivalents	—	(1)
V. Decrease in cash and cash equivalents	(1,257)	(1,202)
VI. Cash and cash equivalents at beginning of year	<u>4,641</u>	<u>3,384</u>
VII. Cash and cash equivalents at end of the period	<u>3,384</u>	<u>2,182</u>

(Notes)

1. Consolidated financial statements of the SCN Group are based on the standards conforming with the Generally Accepted Accounting Principles in Japan.

(For reference)

	<b>(Millions of yen)</b>		
	Fiscal year ended March 31, 2003	<b>Fiscal year ended March 31, 2004</b>	Change (%)
Increase in fixed assets	44	<b>32</b>	(27.5)
Increase in intangible assets	562	<b>942</b>	67.5
Depreciation of fixed assets*	133	<b>110</b>	(17.2)
Amortization of intangible assets*	602	<b>657</b>	9.3
	Three-months ended March 31, 2003	<b>Three-months ended March 31, 2004</b>	Change (%)
Increase in fixed assets	11	<b>2</b>	(80.5)
Increase in intangible assets	124	<b>197</b>	58.4
Depreciation of fixed assets*	34	<b>35</b>	1.6
Amortization of intangible assets*	142	<b>164</b>	15.4

\* Includes extraordinary depreciation of fixed assets, which is included in loss on decided withdrawal from certain operations, and loss on impairment of long-lived assets (excluding those related to leased assets).

## **Strategy and Outlook**

### **(a) Basic management aims**

Since starting Internet connection services under the name of “So-net” in January of 1996, the SCN has strived to offer a new style of network services. The SCN offers various services including a gratifying communications environment and uniquely appealing contents.

Going forward, aiming towards the creation of corporate value and new growth in the 21st century, the SCN has raised up since October 2002 its new slogan “Sony Fun Broadband,” based on a recognition of the importance of strengthening cooperation within the Sony Group in the expanding Internet market. This expresses the intention of the SCN to offer customers services including Sony Group electronic devices and game, music, pictures, and financial services in a broadband Internet environment that is truly always connected. This is the SCN management’s basic aim.

Also, during the year under review, the SCN worked to deepen its services such as by offering a service aimed at televisions.

### **(b) Basic policy for distribution of earnings**

The SCN believes that as well as working to establish and strengthen its corporate foundation, it must also work to aggressively respond to the Internet marketplace, which is characterized by rapid growth in demand for always-on broadband connections and intensifying competition to acquire share. The SCN believes that in order to rapidly ready businesses that respond to these trends, it should manage its operations by expanding cash flow, and by fully solidifying its financial base and retained earnings. For these reasons, for the time being, the SCN does not plan to distribute earnings to SCN shareholders.

### **(c) The view about the reduction in an investment unit**

The reduction in an investment unit is not examined.

### **(d) Current challenges**

Given the business environment in the Internet world that is shifting towards dedicated-line broadband connections, the SCN is working to increase the satisfaction of customers, including the continuous protection of customer information, and is striving to make the advance of broadband the focus of its greatest efforts.

In terms of individual business areas, the SCN is carrying out the following activities:

#### ***a) ISP services***

SCN connection services include a variety of user offerings such as dial-up connections, wireless, ADSL, and FTTH. In the area of FTTH services, which are particularly expected to spread in the future, the SCN is cooperating with NTT, TEPCO, Chubu Electric, and U’s Communications Corp. to cope with different customers’ area, residential departmentalization, and charges. By offering a wide selection of services, such as those aimed at televisions as well as personal computers, the SCN intends to expand further its subscriber base.

#### ***b) Content and services***

By cooperating with the Sony Group, the SCN aims to develop and offer contents and services focused on broadband, including services aimed at televisions. For content and other services, the SCN is striving to increase the revenue and profitability of content by integrating content, e-commerce, and advertising in a way that fully takes into account the degree of use, profitability, and page views.

#### ***c) Cooperation with the Sony Group***

The SCN is working to cooperate with the Sony Group in terms of Sony electronic devices and “So-net” connection services and payment and settlement platforms. The SCN intends to deepen cooperation with the Sony Group, as will be reflected in new products and services. Already, the SCN is striving to strengthen cooperation with the Sony Group by starting a service aimed at televisions.

***d) Investment aims***

The SCN is seizing the challenge to focus on investments in content and services aimed at dedicated-line broadband. The SCN aims to carry out investments for the planning and development of content and services, their procurement and aggregation, and the acquisition of distribution rights, whether internally, by subsidiaries, or by affiliated companies, while at the same time, working to move forward with future investments by clearly setting out profitability and investment objectives.

***e) Securing customers’ private information***

Since its establishment, the SCN has aggressively strived to keep customers’ private information secure by organizing an independent internal unit for that area and by establishing a monitoring system for when operations-related customer information is acquired and distributed. Furthermore, in November 1999, the SCN achieved the “Privacy Mark” for protection of customer information, the first in the industry to pass this hurdle. Also, the SCN established an Information Security Management System (ISMS) which in June 2003 attained international certification (BS7799-2:2002) as well as conformation with domestic ISMS standards. In this way, the SCN is working towards a system that sufficiently manages and protects consumers’ private information.

**(e) Fundamental policies regarding corporate governance and related measures, implementation**

In regards to the corporate governance of the SCN, the basic aims of the Sony Group are as follows.

The SCN is a subsidiary the performance of which is linked to a tracking stock issued by Sony Corporation. As a subsidiary of Sony Corporation, which in actuality has 100% of the voting rights, matters at the SCN’s General Shareholders’ Meeting are all controlled by Sony Corporation. Furthermore, through the directors’ nominations at the General Shareholders’ Meeting, Sony Corporation indirectly controls the board of directors of the SCN.

On the other hand, the directors of Sony Corporation have a fiduciary duty to Sony Corporation and bear a responsibility to work to maximize the corporate value of Sony Corporation, which includes the SCN and the other individual companies of the Sony Group. In view of the definition of the SCN as within the Sony Group, measures to maximize the corporate value of Sony Corporation and measures to maximize the corporate value of the SCN can be thought of as parallel in many cases. However, in situations where within the Sony Group there is the possibility of competition with the SCN as well as cases where the supply of the Sony Group’s limited management resources is to those businesses, then it cannot be denied that there is the possibility that there will be cases where the interests of the overall Sony Group and the interests of the SCN are not parallel. In such a case, as a result of working to maximize the corporate value of the overall Sony Group including the SCN, there is the possibility of a negative impact on the corporate value of the SCN, stemming from such a limitation on a growth opportunity of the SCN.

Based on these possibilities, Sony Corporation has established the following basic aims regarding the SCN.

**i) Basic management aims of the Sony Corporation Board of Directors**

- Indicators of management judgment:

One role of the Board of Directors of Sony Corporation is to coordinate the interests within the Group and carry out management judgment to maximize corporate value of the overall Sony Group. When the case arises that the interests of the SCN and another subsidiary or business unit of Sony Corporation are in conflict, then it is the aim to carry out an appropriate decision that maximizes the corporate value of the Sony Group and does not unreasonably harm the interests of the shareholders.

- Distribution of business opportunities and management resources, dealing with competing businesses:

When carrying out the distribution of business opportunities and management resources within the Group, the Board of Directors of Sony Corporation aims to carry out appropriate management decisions, examining whether to distribute to the SCN or another Group business so that the interests of the entire Sony Group can be increased.

Furthermore, in the development of future businesses, in the case that there exists businesses within the group where their operations replicate that of the SCN, and that it is thought that the competition is having a major impact on the corporate value of the entire Sony Group, then the board of directors and the management entities involved will work to properly adjust the matter.

- Matters for Sony Corporation's Prior Approval:

As for matters relating to SCN management, the SCN Board of Directors carries out decisions of its intentions, but for important matters relating to the management of the entire Sony Group, before the SCN carries out its operational intentions, it must get the approval of Sony Corporation.

For example, matters which fall under this category include something which greatly affects the corporate value of the Sony Group, where there is necessary close cooperation with Sony Corporation or a Sony Group business, or when there is concern that something will be contrary to profitability within the Group.

## ii) Relationship of Sony Corporation and the SCN

- Dividend policy of the SCN:

Under the set terms of the articles of incorporation, Sony Corporation may pay a dividend for the tracking stock where the dividend amount is that which the SCN Board of Directors has proposed as a distribution of the SCN's earnings. The dividend policy of the SCN is decided by the SCN's Board of Directors. The approval beforehand of Sony Corporation is not necessary.

- Disclosure of the SCN:

As long as the subsidiary tracking stock is listed, Sony Corporation plans to disclose the financial information of the SCN each quarter, while also disclosing the financial accounts of the SCN in Sony Corporations's *Yuka Shoken Hokokusho* and *Hanki Hokokusho* (annual and semi-annual financial reports), as is in accordance with the law.

## iii) Summary of implementation of measures relating to corporate governance of the SCN:

The SCN, as a corporation which has adopted the auditing system, has a total of seven directors, including four outside directors. There are also three auditors, all of whom are elected outside auditors. The outside directors include three from Sony Corp. and one from Sony Music Entertainment (Japan) Inc., which is an affiliated company of Sony Corp. The outside auditors include two from Sony Corp. (of which one is a full-time auditor) and one from Sony Finance International, Inc., which is a shareholder of the SCN. With this system of outside directors and auditors, the SCN aims for a corporate governance structure characterized by "checks and balances."

Also, the executive officer system has been introduced within the SCN, and in total there are eight officers. Within those are three directors who serve concurrently as executive officers, and five who are full-time executive officers.

(f) Fundamental policies regarding relations with related parties (such as parent company)

i) Regarding personnel issues

Regarding personnel issues with Sony Corp., for directors it is as stated above in (e)“iii.” For employees, the SCN is defined as being within the Sony Group and predicated on the viewpoint of securing human resources and maintaining flexibility with human resources.

ii) Regarding transactional relations

Sony Corp., in terms of the entire Sony Group, works to use the capital of the Sony Group companies by concentrating resources (concentration of cash scheme), with the goal of more advantageously using working capital. The SCN as well is part of this scheme and deposits its funds with the affiliated company Sony Global Treasury Services PLC. As of the end of March 2004, the transactions of each Sony Group company had been set forth in “Transactional Relations between Related Parties.”

iii) Regarding contracts related to trademarks and patents, and royalties

The SCN’s brands that it uses for its services, such as “So-net” and “Smash” are trademarks that belong to Sony Corp. The SCN has contracted with Sony Corp. regarding exclusive usage rights to the trademarks for “So-net” and “Smash.” Also, while making use of extensive patent assets held by Sony Corp., in order to minimize the possibility of litigation by other companies for patent rights infringement, there are contracts for comprehensive cross-licensing with Sony Corp. for patents and other intellectual property.

(g) Other important items regarding company management

Recently, society has begun to look critically at industries that manage customer private data, such as the transfer of subscriber data. This is a trend not just limited to the industries that are related to the SCN’s activities.

The SCN took the lead before other companies in November 1999 in setting up a mechanism for a system for securing individuals’ private data and achieved the JIS standard for protection of consumer data, the “Privacy Mark.” The SCN places the handling of customers’ private data in a privacy manager in each division. At the same time, the SCN has established a central department for integrating company-wide privacy policies. With this department as the center, the SCN carries out thorough employee education and implements, through each of the privacy managers, the most appropriate management methods for private data. In this way, the SCN is working to keep customers’ private data secure on an ongoing basis.

(h) Risk management

At the present time, the main risk factors for the SCN are as follows:

i) The business environment in which the SCN operates

The SCN is not merely an Internet service provider, but it is a business which offers a wide-range of services including contents and such. For that reason, the SCN competes with various other companies in areas including not just Internet connection services, but also communications services, broadcasting services, and other areas. Competition is intense, especially in the area of Internet connection services, such as FTTH and ADSL. It is possible that the SCN’s revenue and

profitability will decline as a result of competition stemming from these areas. In addition, there is also the possibility that there may be unavoidable expenses related to price competition or the building of market share, such as marketing and promotion costs. There is the possibility that there will be a large negative impact on the SCN's financial performance.

ii) Revenue structure

The proportion of the SCN's total sales that stem from connection services was 80.5% during the year ended March 31, 2004. The profitability of these connection services is greatly impacted by such factors as trends in the number of subscribers, cost trends for such services (such as expenses related to promotional campaigns), and developments in communication line costs. Furthermore, given these circumstances where a majority of revenue is dependent on connection services, it is expected that those unpredictable factors will impact SCN's financial results in the future.

iii) Legal environment for the Internet

The SCN's Internet connection service business is impacted by regulations based on the Telecommunication Business Law. In addition, while regulations from such laws as the Unauthorized Computer Access Law and the ISP Law do not directly impact Internet-related businesses, there are regulations that indirectly concern communication methods such as the Internet. Also, in the unfolding area of e-commerce, laws protecting consumers such as the Consumer Contract Act, the Specific Commercial Transaction Act, Act about payment in installments, Antique business Act, and the Act against Unjustifiable Premiums and Misleading Representations involve regulations that impact the SCN. If the SCN were to violate any of these laws, the reputation of the SCN might be damaged, and there could be a negative impact on future operations. Also, there is the possibility of having to establish a structure for observing new laws if there were revisions in these laws.

Also, there is the possibility of unavoidable circumstances where the SCN has to bear some legal risk. A legal judgment, including the jurisdiction or legal basis for such, against the SCN cannot be accurately forecast, such as in the case that some kind of legal trouble were to arise in the business operations of the SCN.

Furthermore, there is the possibility of restrictions on future operations of the SCN, in terms of laws and regulations in countries, including Japan, in regards to the Internet and e-commerce.

iv) Possibility of infringement upon intellectual property

Given that the SCN develops businesses related to the Internet, there is the possibility that there could be infringement on other companies' intellectual property, such as technology patents and business model patents, trademarks, or design rights. The SCN works hard to make sure that such violations of intellectual property rights do not occur, but there is the possibility of having to shoulder significant compensation for damages in the case that some company's intellectual property rights were violated. Also, there is the possibility that there will be pressure on future earnings due to the necessity of paying licensing fees in the case that another company develops technology or another company's business model becomes the standard.

v) Securing and developing human resources

In terms of developing the SCN's businesses, it is necessary to secure personnel that have creative and technological skills. However, in the area of Internet-related businesses, turnover of personnel is high and it is possible that in the future the SCN will not be able to secure the necessary human resources. Furthermore, in the SCN are many people who have transferred from various Sony

Group companies, and while the SCN is working to secure flexible personnel arrangements, it is possible that the SCN will have trouble securing personnel as a result of policies designed to maximize the corporate value of the entire Sony Group. The SCN is also working to develop human capital within the company, but in the case that the SCN is unable to secure or develop sufficient human resources, there could be a negative impact on the future business developments of the SCN.

vi) System for operating servers

The SCN has laid out a system for managing all the servers that are used to manage customer data and settlement 24 hours a day, 365 days a year. With respect to the unpredictability of accidents, the SCN has back-ups for important servers depending on the substance of a service. However, there is the possibility of an inability to use the servers if there were an earthquake, fire, or other natural disaster, or a destructive act that damages the service offerings. In such a case, there is the possibility of a large negative impact on the continuation of the SCN's operations.

vii) Operation of call centers

For the SCN, appropriately responding to customer inquiries is considered indispensable in order to acquire and keep So-net subscribers. There is a dependence on temporary staff, who are the majority of personnel in SCN call centers. Regarding temporary staff who start work in call centers, while the SCN is working to continue to improve quality, such as by carrying out sufficient training, there is the possibility that service levels will decline for some reason, such as if there were a shortage of call center staff. In such a case, there is the possibility of a negative impact on the SCN's financial results.

(i) Regarding compulsory retirement of the subsidiary tracking stock or the compulsory conversion into common stock of the parent company (Sony Corporation)

At the present time, unless there are significant changes in the direction of the corporate strategy of the entire Sony Group or in the way that the SCN is defined within the Sony Group, or unless there are significant changes in a business environment which includes a variety of factors such as the growth of the SCN, there are no plans to carry out compulsory retirement or conversion into common stock three years after the issuance of the subsidiary tracking stock, that is to say, on June 20, 2004.

### (j) Forecast of Consolidated Results

Regarding the forecast of the consolidated results for the fiscal year ending March 31, 2005, the SCN has the goal of achieving operating profitability.

- It is expected that there will be a further acceleration in FTTH-related services (including acquiring new subscribers).
- The SCN plans to expand usability by investing in new businesses (mainly value-added broadband contents), in particular services aimed at television. At the same time, the SCN aims to carefully select investments and will focus on profitability.
- The SCN will work to strengthen the overall management structure.

The SCN announces the following forecast for consolidated results:

<u>Consolidated Results</u>		(millions of yen) <u>Change from previous year</u>
Sales	40,000	+4.8%
Operating income	100	---
Ordinary income	100	---
Net income	50	---

The above forecast takes into account the following expected factors:

- It is expected that the number of So-net subscribers at the end of the year ending March 31, 2005 will be 2.35 million, an increase over the year earlier period of 50,000.
- Within the above total, the number of broadband subscribers is targeted to 700,000, an increase of 150,000 over the year earlier period.
- Regarding expected sales by category:

		(change from previous year)
ISP services	30,800	+0.2%
Internet-related services	8,100	+24.2%
Merchandise sales	1,100	+20.6%

As for ISP services, it is expected that competition for new subscribers will intensify and that the rate of growth will be slow. As for Internet-related services, it is expected that sales of broadband content will increase, and it is expected that subsidiaries' results will improve. As for Merchandise sales, it is expected that sales of goods connected with "Content" will increase.

### **Cautionary statement:**

Statements made in this release with respect to Sony Corporation and Sony Communication Network's ("SCN") current plans, estimates, strategies and beliefs and other statements that are not historical facts are forward-looking statements about the future performance of SCN. These statements are based on management's assumptions and beliefs in light of the information currently available to it. Therefore, SCN cautions you that a number of important risks and uncertainties could cause actual results to differ materially from those discussed in the forward-looking statements, and therefore you should not place undue reliance on them.