DTS Corporation (Formerly Data Communication System Co., Ltd.) and Subsidiaries

Unaudited Semiannual Consolidated Financial Statements for the Six Months Ended September 30, 2003 and 2002

DTS Corporation (Formerly Data Communication System Co., Ltd.)
and Subsidiaries

Semiannual Consolidated Balance Sheets
September 30, 2003 and 2002—Unaudited

ASSETS	Millions of Yen 2003	Millions of Yen 2002	Thousands of U.S. Dollars (Note 1) 2003
CURRENT ASSETS:			
Cash and cash equivalents	¥ 5,657	¥ 7,872	$ 50,849
Time deposits		500	
Receivables:			
Trade accounts	6,447	6,493	57,950
Other	17	15	153
Allowance for doubtful receivables	(4)	(11)	(36)
Inventories (Note 3)	1,337	1,135	12,018
Deferred tax assets	916	640	8,234
Prepaid expenses and other current assets	355	132	3,191
Total current assets	14,725	16,776	132,359
PROPERTY, PLANT AND EQUIPMENT:			
Land	7,066	5,943	63,515
Buildings and structures	4,929	4,924	44,305
Furniture and fixtures	1,134	1,073	10,193
Construction in progress	260		2,337
Other	33	39	297
Total	13,422	11,979	120,647
Accumulated depreciation	(2,916)	(2,684)	(26,211)
Net property, plant and equipment	10,506	9,295	94,436
INVESTMENTS AND OTHER ASSETS:			
Investment securities (Note 4)	1,713	1,187	15,398
Goodwill	81	142	728
Guarantee money deposit	327	387	2,939
Deferred tax assets	446	511	4,009
Other assets	389	444	3,497
Total investments and other assets	2,956	2,671	26,571
TOTAL	¥ 28,187	¥ 28,742	$ 253,366

LIABILITIES AND SHAREHOLDERS' EQUITY	Millions of Yen 2003	Millions of Yen 2002	Thousands of U.S. Dollars (Note 1) 2003
CURRENT LIABILITIES:			
Current portion of long-term debt (Note 5)		¥ 1,723	
Payables:			
Trade accounts	¥ 1,682	1,876	$ 15,119
Other	634	605	5,699
Income taxes payable	676	646	6,076
Accrued expenses	1,981	1,680	17,807
Other current liabilities	495	531	4,449
Total current liabilities	5,468	7,061	49,150
LONG-TERM LIABILITIES:			
Liability for employees' retirement benefits	670	514	6,023
Retirement allowances for directors and corporate auditors	161	230	1,447
Total long-term liabilities	831	744	7,470
MINORITY INTERESTS	391	240	3,515
SHAREHOLDERS' EQUITY (Note 6):			
Common stock—authorized, 18,000,000 shares; issued, 12,611,133 shares in 2003 and 2002	6,113	6,113	54,948
Capital surplus	6,191	6,191	55,649
Retained earnings	9,995	8,877	89,843
Net unrealized gain (loss) on available-for-sale securities	188	(4)	1,690
Treasury stock—at cost, 380,806 shares in 2003 and 115,574 shares in 2002	(990)	(480)	(8,899)
Total shareholders' equity	21,497	20,697	193,231
TOTAL	¥ 28,187	¥ 28,742	$ 253,366

See notes to semiannual consolidated financial statements.

DTS Corporation (Formerly Data Communication System Co., Ltd.) and Subsidiaries

Semiannual Consolidated Statements of Income
Six Months Ended September 30, 2003 and 2002—Unaudited

	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2003	2002	2003
NET SALES	¥ 17,437	¥ 17,402	$ 156,737
COST OF SALES (Note 8)	14,462	14,244	129,995
Gross profit	2,975	3,158	26,742
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES (Note 8)	1,651	1,568	14,841
Operating income	1,324	1,590	11,901
OTHER INCOME (EXPENSES):			
Interest and dividend income	24	8	216
Interest expense	(3)	(15)	(27)
Other—net	(21)	40	(189)
Other income—net		33	
INCOME BEFORE INCOME TAXES AND MINORITY INTERESTS	1,324	1,623	11,901
INCOME TAXES (Note 7):			
Current	675	642	6,067
Deferred	(98)	84	(881)
Total income taxes	577	726	5,186
MINORITY INTERESTS IN NET INCOME	18	7	162
NET INCOME	¥ 729	¥ 890	$ 6,553

	Yen		U.S. Dollars
PER SHARE OF COMMON STOCK (Notes 2.m and 10):			
Net income	¥ 59.28	¥ 71.20	$ 0.53
Fully diluted net income		71.20	

See notes to semiannual consolidated financial statements.

DTS Corporation (Formerly Data Communication System Co., Ltd.)
and Subsidiaries

Semiannual Consolidated Statements of Shareholders' Equity
Six Months Ended September 30, 2003 (Unaudited) and Year Ended March 31, 2003

	Issued Number of Shares of Common Stock	Millions of Yen: Common Stock	Capital Surplus	Retained Earnings	Net Unrealized Gain (Loss) on Available-for-sale Securities	Treasury Stock
BALANCE, APRIL 1, 2002	12,609,633	¥ 6,111	¥ 6,189	¥ 8,691	¥ (3)	¥ (480)
Net income				1,926		
Cash dividends, ¥57 per share				(712)		
Bonuses to directors and corporate auditors				(142)		
Exercise of warrants	1,500	2	2			
Net decrease in unrealized loss on available-for-sale securities					2	
Increase in treasury stock (73,996 shares)						(148)
BALANCE, MARCH 31, 2003	12,611,133	6,113	6,191	9,763	(1)	(628)
Net income				729		
Cash dividends, ¥35.0 per share				(435)		
Bonuses to directors and corporate auditors				(62)		
Net increase in unrealized gain on available-for-sale securities					189	
Increase in treasury stock (191,384 shares)						(362)
BALANCE, SEPTEMBER 30, 2003	12,611,133	¥ 6,113	¥ 6,191	¥ 9,995	¥ 188	¥ (990)

	Thousands of U.S. Dollars (Note 1): Common Stock	Capital Surplus	Retained Earnings	Net Unrealized Gain (Loss) on Available-for-sale Securities	Treasury Stock
BALANCE, MARCH 31, 2003	$ 54,948	$ 55,649	$ 87,757	$ (9)	$ (5,645)
Net income			6,553		
Cash dividends, $0.31 per share			(3,910)		
Bonuses to directors and corporate auditors			(557)		
Net increase in unrealized gain on available-for-sale securities				1,699	
Increase in treasury stock					(3,254)
BALANCE, SEPTEMBER 30, 2003	$ 54,948	$ 55,649	$ 89,843	$ 1,690	$ (8,899)

See notes to semiannual consolidated financial statements.

DTS Corporation (Formerly Data Communication System Co., Ltd.) and Subsidiaries

Semiannual Consolidated Statements of Cash Flows
Six Months Ended September 30, 2003 and 2002—Unaudited

	Millions of Yen		Thousands of U.S. Dollars (Note 1)
	2003	2002	2003
OPERATING ACTIVITIES:			
Income before income taxes and minority interests	¥ 1,324	¥ 1,623	$ 11,901
Adjustments for:			
Income taxes paid	(1,096)	(1,487)	(9,852)
Depreciation and amortization	174	205	1,564
Changes in assets and liabilities:			
Decrease in receivables	1,083	912	9,735
Increase in inventories	(594)	(699)	(5,339)
Increase in prepaid expenses and other current assets	(262)	(50)	(2,355)
Decrease in payables	(722)	(839)	(6,490)
Increase in accrued expenses	282	183	2,535
Decrease in other current liabilities	(59)	(247)	(530)
Increase (decrease) in liability for retirement benefits	14	(287)	126
Other—net	195	(173)	1,752
Total adjustments	(985)	(2,482)	(8,854)
Net cash provided by (used in) operating activities	339	(859)	3,047
INVESTING ACTIVITIES:			
Payment for purchases of property, plant and equipment	(346)	(139)	(3,110)
Payment for purchases of marketable and investment securities	(5)	(500)	(45)
Increase in time deposits		(500)	
Proceeds from sale of consolidated subsidiary securities	104		935
Other—net	(2)	(3)	(18)
Net cash used in investing activities	(249)	(1,142)	(2,238)
FINANCING ACTIVITIES:			
Redemption of bonds	(700)	(300)	(6,292)
Cash dividends paid	(433)	(558)	(3,892)
Payment for purchase of treasury stock	(362)		(3,254)
Other—net	(3)	(9)	(27)
Net cash used in financing activities	(1,498)	(867)	(13,465)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(1,408)	(2,868)	(12,656)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	7,065	10,740	63,505
CASH AND CASH EQUIVALENTS, END OF PERIOD	¥ 5,657	¥ 7,872	$ 50,849

See notes to semiannual consolidated financial statements.

1. BASIS OF PRESENTING SEMIANNUAL CONSOLIDATED FINANCIAL STATEMENTS

The accompanying unaudited semiannual consolidated financial statements of DTS Corporation (the "Company") and subsidiaries have been prepared in accordance with the provisions set forth in the Japanese Securities and Exchange Law (the "Law"), and in conformity with the provisions of "Accounting and Reporting Standards of Semiannual Consolidated Financial Statements" (the "Standards") issued by the Business Accounting Council, an advisory body to the Financial Services Agency, designated to set accounting standards for business enterprises in Japan, which are different in certain respects as to application and disclosure requirements of the International Financial Reporting Standards. The unaudited semiannual consolidated financial statements are not intended to present the financial position, results of operations and cash flows in accordance with accounting principles and practices generally accepted in countries and jurisdictions other than Japan.

In preparing these unaudited semiannual consolidated financial statements, certain reclassifications and rearrangements have been made to the semiannual consolidated financial statements issued domestically in order to present them in a form which is more familiar to readers outside Japan. In addition, certain reclassifications have been made in the 2002 financial statements to conform to the classifications used in 2003.

The unaudited semiannual consolidated financial statements are stated in Japanese yen, the currency of the country in which the Company is incorporated and operates. The translations of Japanese yen amounts into U.S. dollar amounts are included solely for the convenience of readers outside Japan and have been made at the rate of ¥111.25 to $1, the rate of exchange at September 30, 2003. Such translations should not be construed as representations that the Japanese yen amounts could be converted into U.S. dollars at that or any other rate.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a. ***Consolidation***—The semiannual consolidated financial statements include the accounts of the Company and all subsidiaries (together, the "Group").

Under the control concept, those companies in which the Company, directly or indirectly, is able to exercise control over operations are fully consolidated.

The excess of the cost of an acquisition over the fair value of the net assets of the acquired subsidiary at the date of acquisition is being amortized over a period of five years. All significant intercompany balances and transactions have been eliminated in consolidation. All material unrealized profit included in assets resulting from transactions within the Group is eliminated.

b. ***Cash Equivalents***—Cash equivalents are short-term investments that are readily convertible into cash and that are exposed to insignificant risk of changes in value. Cash equivalents include demand deposits, time deposits and other short-term investments, all of which mature or become due within three months of the date of acquisition.

c. ***Inventories—***Merchandise is stated at cost determined by the moving-average method. Work in process is stated at cost determined by the specific identification method. Supplies are stated at cost determined by the last purchase cost method.

d. ***Property, Plant and Equipment—***Property, plant and equipment are stated at cost. Depreciation is computed basically by the declining-balance method at rates based on the estimated useful lives of the assets. The range of useful lives is principally from 3 to 50 years for buildings and structures and from 2 to 20 years for furniture and fixtures.

   Assets with an acquisition cost from ¥100,000 to ¥200,000 are depreciated by the straight-line method over three years.

e. ***Software Costs—***Software development costs, incurred through the completion of a Beta version of specific software for sale to the market, are charged to income when incurred. Such costs incurred subsequent to the completion of the Beta version are deferred and amortized at the greater of either the amount to be amortized in proportion of the actual sales volume of the software during the current period to the estimated total sales volume over the estimated salable years of the software up to three years or the amount to be amortized by the straight-line method over such salable years. Most of purchased software costs are charged to income as incurred because of the uncertainty that such costs will be recovered from related future economic benefits.

f. ***Investment Securities—***Available-for-sale securities with market value are stated at fair value at each balance sheet date, with unrealized gains and losses, net of applicable taxes, reported in a component of shareholders' equity. The cost of securities sold is determined based on the moving-average method.

   Non-marketable available-for-sale securities are stated at cost being determined by the moving-average method.

g. ***Employees' Pension Plan—***The Company has a contributory and a non-contributory funded pension plans covering substantially all of its employees. The subsidiaries also have a contributory or a non-contributory funded pension plan covering substantially all of their employees. Employees whose service with the Group is terminated are, under most circumstances, entitled to retirement and pension benefits determined by reference to basic rates of pay at the time of termination, length of service and conditions under which the termination occurs. If the termination is involuntary, caused by retirement at the mandatory retirement age or caused by death, the employee is entitled to greater payment than in the case of voluntary termination.

   The Group accounted for the liability for retirement benefits based on projected benefit obligations and plan assets at the balance sheet date for its non-contributory funded pension plans. The costs of the pension plan, based on actuarial computations of current and future employee benefits, are charged to operations. Actuarial gain or loss is being amortized over five years and its recognition starts from the following fiscal period.

   The policy of the Company and a subsidiary for its contributory pension plan is to charge operations normal costs to the pension plan as accrued on the basis of an accepted actuarial method plus amortization of prior service costs.

   Effective January 1, 2004, the Company will amend the non-contributory funded pension plan to a benefit plan of advance retirement payments and a defined contribution pension plan. The effect of this amendment will be to increase income before taxes by approximately ¥155 million for the year ending March 31, 2004.

h. ***Retirement Allowances for Directors and Corporate Auditors*—**Directors and corporate auditors are generally entitled to receive lump-sum payments based on compensation at the time of resignation and the number of years of service when they resign from the Company. The accrued provisions are not funded and any amounts payable to directors and corporate auditors upon resignation are subject to the approval of the shareholders. The provision for severance payments is calculated to state the severance liability at the amount that would be payable if all directors and corporate auditors were to resign at the balance sheet date.

i. ***Research and Development Costs*—**Research and development costs of the Company are charged to income as incurred.

j. ***Leases*—**All leases are accounted for as operating leases. Under Japanese accounting standards for leases, finance leases that deem to transfer ownership of the leased property to the lessee are to be capitalized, while other finance leases are permitted to be accounted for as operating lease transactions if certain "as if capitalized" information is disclosed in the notes to the lessee's financial statements.

k. ***Income Taxes*—**Deferred income taxes are recorded to reflect the impact of temporary differences between assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes, based on the asset and liability method. These deferred taxes are measured by applying currently enacted tax laws to the temporary differences.

l. ***Appropriations of Retained Earnings*—**Appropriations of retained earnings are reflected in the semiannual consolidated financial statements for the following year upon shareholders' approval.

m. ***Per Share Information*—**The Company adopts the accounting standard for earnings per share of common stock issued by the Accounting Standards Board of Japan. Under the standard, basic net income per share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding in each period, retroactively adjusted for stock splits.

Diluted net income per share reflects the potential dilution that could occur if warrants or stock options were exercised. Diluted net income per share of common stock assumes full exercise of the outstanding warrants and stock options at the beginning of the period. Diluted net income per share is not disclosed because it is anti-dilutive in 2003.

3. INVENTORIES

Inventories at September 30, 2003 and 2002, consisted of the following:

	Millions of Yen		Thousands of U.S. Dollars
	2003	2002	2003
Merchandise	¥ 27	¥ 156	$ 243
Work in process	1,302	964	11,703
Supplies	8	15	72
Total	¥ 1,337	¥ 1,135	$ 12,018

4. INVESTMENT SECURITIES

Investment securities as of September 30, 2003 and 2002, consisted of non-current equity securities.

The carrying amounts and aggregate fair values of investment securities at September 30, 2003 and 2002, were as follows:

	Millions of Yen			
September 30, 2003	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as available-for-sale equity securities	¥ 184	¥ 314		¥ 498
September 30, 2002				
Securities classified as available-for-sale equity securities	163		¥ 9	154

	Thousands of U.S. Dollars			
September 30, 2003	Cost	Unrealized Gains	Unrealized Losses	Fair Value
Securities classified as available-for-sale equity securities	$ 1,654	$ 2,823		$ 4,477

Available-for-sale securities whose fair value is not readily determinable as of September 30, 2003 and 2002, were as follows:

	Carrying Amount		
	Millions of Yen		Thousands of U.S. Dollars
	2003	2002	2003
Investment securities, available-for-sale equity securities	¥ 1,215	¥ 1,033	$ 10,921

5. SHORT-TERM AND LONG-TERM DEBT

Short-term and long-term debt at September 30, 2002, consisted of the following:

	Millions of Yen
	2002
Unsecured 2.0% bonds, due December 2002	¥ 23
Unsecured 2.0% bonds, due June 2004	700
Unsecured 1.38% bonds, due October 2005	1,000
Total	1,723
Less current portion	(1,723)
Long-term debt, less current portion	

On September 4, 2002, the Board of Directors of the Company approved the redemption of the unsecured 2.0% bonds, due June 2004 and the unsecured 1.38% bonds. The 1.38% bonds were redeemed on October 11, 2002 and the 2.0% bonds, due June 2004 were redeemed on June 13, 2003.

6. SHAREHOLDERS' EQUITY

The Japanese Commercial Code (the "Code") provides that whereby common stock par value was eliminated resulting in all shares being recorded with no par value and at least 50% of the issue price of new shares is required to be recorded as common stock and the remaining net proceeds as additional paid-in capital, which is included in capital surplus. The Code permits companies, upon approval of the Board of Directors, to issue shares to existing shareholders without consideration as a stock split. Such issuance of shares generally does not give rise to changes within the shareholders' accounts.

The Code also provides that an amount at least equal to 10% of the aggregate amount of cash dividends and certain other appropriations of retained earnings associated with cash outlays applicable to each period shall be appropriated as a legal reserve (a component of retained earnings) until such reserve and additional paid-in capital equals 25% of common stock. The amount of total additional paid-in capital and legal reserve that exceeds 25% of the common stock may be available for dividends by resolution of the shareholders. In addition, the Code permits the transfer of a portion of additional paid-in capital and legal reserve to the common stock by resolution of the Board of Directors.

The Code eliminated restrictions on the repurchase and use of treasury stock allowing Japanese companies to repurchase treasury stock by a resolution of the shareholders at the general shareholders meeting and dispose of such treasury stock by resolution of the Board of Directors beginning April 1, 2002. The repurchased amount of treasury stock cannot exceed the amount available for future dividend plus amount of common stock, additional paid-in capital or legal reserve to be reduced in the case where such reduction was resolved at the general shareholders meeting.

Dividends are approved by shareholders at a meeting held subsequent to the fiscal year to which the dividends are applicable. Semiannual interim dividends may also be paid upon resolution of the Board of Directors, subject to certain limitations imposed by the Code. On November 18, 2003, the Board of Directors approved interim dividends of ¥15 per share to the shareholders on record as of September 30, 2003.

On September 17, 2002, the Company issued new stock acquisition rights as a stock option plan for the Company's directors, corporate auditors and key employees. The number of shares to be issued is 100,000 shares of common stock of the Company. The exercise period of the options is from October 2002 to June 2012 and the exercise price of the options is ¥3,199.

On August 20, 2003, the Company issued another stock acquisition rights as a stock option plan for the Company's directors, corporate auditors and key employees. The number of shares to be issued is 102,500 shares of common stock of the Company. The exercise period of the options is from October 2003 to June 2013 and the exercise price of the options is ¥2,675.

7. INCOME TAXES

The Group is subject to Japanese national and local income taxes which, in the aggregate, resulted in a normal effective statutory tax rate of approximately 41% and 42% for the periods ended September 30, 2003 and 2002, respectively.

8. LEASES

The Group leases vehicle, furniture and fixtures, software and other assets.

Total rental expenses under the above leases for the six months ended September 30, 2003 and 2002 were ¥28 million ($252 thousand) and ¥29 million, respectively, including ¥24 million ($216 thousand) and ¥23 million of lease payments under finance leases.

Pro forma information of leased property such as acquisition cost, accumulated depreciation, obligation under finance lease, depreciation expense of finance leases that do not transfer ownership of the leased property to the lessee on an "as if capitalized" basis for the periods ended September 30, 2003 and 2002, was as follows:

	Millions of Yen					
	2003			2002		
	Furniture and Fixtures	Software	Total	Furniture and Fixtures	Software	Total
Acquisition cost	¥ 100	¥ 25	¥ 125	¥ 120	¥ 21	¥ 141
Accumulated depreciation	58	7	65	77	6	83
Net leased property	¥ 42	¥ 18	¥ 60	¥ 43	¥ 15	¥ 58

	Thousands of U.S. Dollars		
	2003		
	Furniture and Fixtures	Software	Total
Acquisition cost	$ 899	$ 225	$ 1,124
Accumulated depreciation	522	63	585
Net leased property	$ 377	$ 162	$ 539

Acquisition costs and obligations include the imputed interest expense portion.

Obligations under finance leases:

	Millions of Yen		Thousands of U.S. Dollars
	2003	2002	2003
Due within one year	¥ 21	¥ 25	$ 189
Due after one year	39	33	350
Total	¥ 60	¥ 58	$ 539

Depreciation expense including imputed interest expense under finance leases is ¥13 million ($117 thousand) for the period ended September 30, 2003 and ¥13 million for the period ended September 30, 2002.

Depreciation expense, which is not reflected in the accompanying semiannual consolidated statements of income, is computed by the straight-line method.

9. SEGMENT INFORMATION

The Group was mainly engaged in the information service industry segment. The sales or operating income of that segment accounted for more than 90% of the total consolidated sales or operating income. Other sales or operating income were not significant compared to the above segment. Therefore, information about operations in different industry segments has been omitted. As the Group had no foreign operations and sales to foreign customers, information about geographical segments and sales to foreign customers were not disclosed.

10. NET INCOME PER SHARE

Reconciliation of the differences between basic and diluted net income per share ("EPS") for the six months ended September 30, 2003 and 2002, is as follows:

	Millions of Yen	Thousands of Shares	Yen	U.S. Dollars
Six Months Ended September 30, 2003	Net Income	Weighted-average Shares	EPS	
Basic EPS—Net income available to common shareholders	¥ 729	12,303	¥ 59.28	$ 0.53
Six Months Ended September 30, 2002				
Basic EPS—Net income available to common shareholders	¥ 890	12,495	¥ 71.20	
Effect of dilutive securities—Warrants		1		
Diluted EPS—Net income for computation	¥ 890	12,496	¥ 71.20	

11. SUBSEQUENT EVENT

At the Board of Directors meeting held on September 17, 2003, the directors resolved to sell several land and buildings, which had been used as an employees' dormitory. The sale price and the loss on the sales were approximately ¥235 million ($2,112 thousand) and ¥412 million ($3,703 thousand) in total, respectively, and those contracts were agreed on September and December 2003.

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