

Financial Section

Management's Discussion and Analysis of Results of Operations and Financial Condition

◆ Consolidated Business Results

The economic condition in our service area recovered moderately during FY2016, including recovery in manufacturing activities and housing starts.

Under these circumstances, as a result of diligent efforts to expand city gas use, supply stably and ensure security, the number of gas meters increased by 1.1% from the previous year. The consolidated gas sales volume increased by 1.7% from the previous year and LPG sales volume increased by 4.5%.

Consolidated net sales decreased by 18.6% from the

previous year to ¥390,434 million, mainly due to a decrease in sales unit prices under the Fuel Cost Adjustment System. Cost of sales decreased by 17.1% to ¥230,491 million, mainly due to a decrease in raw material costs, following a decline in crude oil prices. Selling, general and administrative expenses decreased by 3.1% to ¥136,754 million. Consequently, ordinary income decreased by 59.9% to ¥24,490 million. Net income attributable to owners of the parent decreased by 58.7% from the previous year to ¥17,749 million.

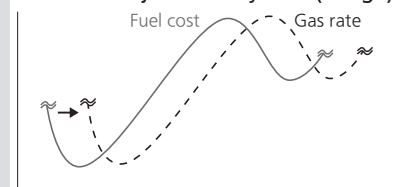
Reference Characteristics of the Gas Rate System

City gas is made from liquefied natural gas (LNG), whose price changes depending on the crude oil price and exchange rates. In Japan, this fluctuation in fuel costs is reflected several months later in the gas fee rates, in accordance with the Fuel Cost Adjustment System.

Accordingly, the impact of fuel cost fluctuations is offset in the long term, but they do affect the operational results of the short term. Specifically, if the LNG price increases, the fuel cost to the Company will increase, negatively affecting

the Company's profit/loss, until the fee charged to customers is adjusted (increased). If the LNG price decreases, fuel costs to the Company will decrease, positively affecting profit/loss status until the fee is adjusted (decreased).

Fuel Cost Adjustment System (Image)



◆ Segment Information

Gas Sales

The number of gas meters increased by 25 thousand to 2,434 thousand during the year.

The total gas sales volume increased 1.7% to 3,974 million m³. In the residential market, sales volume was 745 million m³, an increase of 1.7% from the previous year, mainly due to an increase of the number of customers and lower temperatures in winter. In the non-residential segment, sales volume was 2,975 million m³, an increase of

2.5% from the previous year, mainly due to our marketing efforts to create new gas demand. The volume of wholesale sales to other gas utilities decreased 7.3% to 254 million m³.

Gas sales revenues decreased 24.3% from the previous year to ¥268,748 million, mainly due to a decrease in sales unit prices under the Fuel Cost Adjustment System. Operating income decreased 66.4% to ¥18,794 million.

Gas Appliance Sales and Related Construction

Sales revenues of this segment decreased by 2.5% from the previous year to ¥36,861 million due to a decrease in sales

of non-residential gas appliances, despite an increase in the new construction works. Operating loss was ¥169 million.

LPG and other Energies

Sales of LPG and thermal energy supply businesses, etc. decreased by 3.2% from the previous year to ¥66,457 million. Operating income decreased by 22.1%, to ¥1,534 million. LPG sales volume increased 4.5% from the previous

year to 454 thousand tons. As for sales of electricity, a business we launched in April 2016, the number of applications was 24 thousand at the end of FY2016.

Other

Sales of other businesses, including plant design and construction, and real estate leasing, decreased by 3.5% to

¥37,548 million. Operating income increased by 8.3% to ¥1,737 million.

Financial Section

◆ Financial Position

Assets, Liabilities and Net Assets

Total assets decreased by ¥22,287 million from the end of the previous year. Liabilities decreased by ¥43,902 million. Net assets increased by ¥21,615 million.

As a result, the equity ratio increased from 51.4% in the previous year to 57.6%.

Cash Flows

Net cash provided by operating activities was ¥37,264 million, mainly due to recording of income before income taxes.

Net cash used in investing activities was ¥57,968 million, which was mainly used for facilities investments.

As a result, free cash flow for the year was negative ¥20,703 million.

Net cash used in financing activities was ¥22,962 million, which was mainly used for reduction of interest-bearing debt.

As a result, net cash and cash equivalents as of the end of March 31, 2017 decreased by ¥43,817 million from the same date of the previous year to ¥16,497 million.

Risks

The major risks that have the potential to impact the Group's results of operations and financial condition are described below. Forward-looking statements are based on information available to management as of March 31, 2017.

(a) Impact of change in demand

The sales volume and profitability of the city gas and LPG gas businesses may be affected, positively or negatively, by economic conditions as well as by changes in temperature, such as extreme heat, warm winters, and irregular water-temperature conditions. Also potentially affecting our businesses is the changes in the competitive environment that happens in the wake of full liberalization of the gas market.

(b) Impact of fluctuating fuel costs

LNG is the primary resource for gas production. The supply-demand balance as well as fluctuating crude oil prices and exchange rates can impact the cost of LNG and other resources. Fluctuations in the LNG price are offset by adjustments in the gas sales price made in accordance with the fuel cost adjustment system. However, since there is a time lag until the adjustment is made, the operating results for a given year may be affected by such fluctuations in LNG price. Operating results and financial conditions may be affected by the development of the negotiation of LNG prices.

(c) Impact of changing interest rates and other market conditions

Trends in market interest rates will cause the cost of debt to fluctuate, which may affect income and expenses. However, most of Toho Gas' interest-bearing debt comprises long-term loans and corporate bonds acquired at fixed interest rates. By steadily reducing interest-bearing debt, the Company limits the risks inherent in changing interest rates.

The value of assets held by our group, such as stocks and pensions, may change because of possible fluctuations of stock prices and interest-rate trends. Consequently, profitability of our businesses may be affected, positively or negatively.

(d) Impact of revisions in governmental policies, laws and statutory systems

Any revision in the government's energy policy, environmental policy, law or statutory system may have impact on the operating results of the Toho Gas Group.

(e) Impact of natural disasters

Large-scale natural disasters may have impact on the operating results of the Toho Gas Group, as such disasters may cause damages to the production/supply facilities of the Group and customers' business sites. Unexpected large-scale power failure may also have negative impact on the operating results of the Toho Gas Group.

To prepare for large-scale natural disaster and to minimize resulting damage, the Company has installed in-house power generation facilities, fire-fighting equipment and other disaster control facilities and systems. The earthquake resistance of gas pipes and supply and production facilities has also been improved.

(f) Impact of serious difficulty in procuring gas resources, production or supply process

Serious difficulty in procuring gas resources, production or supply process may have negative impact on the operating results of the Toho Gas Group.

(g) Impact of mission-critical information system

Mission-critical information system may have negative impact on the operating results of the Toho Gas Group.

(h) Impact of serious problems involving customers' gas equipment and appliances

Serious problems involving customers' gas equipment and appliances may result in tangible or intangible damages, including social liabilities, being incurred by the Company.

(i) Impact of quality of products handled and services provided

Problems involving the quality of products handled and services offered by the Toho Gas Group and companies entrusted to sell them on the Group's behalf may result in tangible or intangible damages, including social liabilities, being incurred by the Company.

(j) Impact of changes in overseas investment conditions

Part or all of overseas investments may not be recovered properly as a result of changes in the economic conditions and other factors and such irrecoverability may affect the operating results of the Toho Gas Group.

Changes in rules and laws, and business practices in countries where Group companies are to commence business may cause delays and stall their business operations, and lead to additional business expenses.

(k) Impact of non-compliance

If the Company or any related party to the Company breaches any law, agreement or conducts any act against corporate ethics or social norms, this may result in tangible or intangible damages, including social liabilities, being incurred by the Company.

(l) Impact of information leak

If customers' personal information kept and managed by the Toho Gas Group leaks outside the Group, this may result in tangible or intangible damages, including social liabilities, being incurred by the Company.

(m) Impact of pandemic of new-type influenza or other infectious disease

Pandemic of new-type influenza or other infectious disease may have negative impact on the operating results of the Toho Gas Group.

Consolidated Balance Sheets

TOHO GAS CO., LTD. and Consolidated Subsidiaries
March 31, 2017 and 2016

Assets	Millions of yen		Thousands of U.S. dollars (Note 1)
	2017	2016	2017
Property, plant and equipment (Notes 7 and 15):			
Production facilities	¥262,830	¥241,623	\$2,346,696
Distribution facilities.....	905,058	876,942	8,080,875
Service and maintenance facilities	70,050	69,147	625,446
Other facilities	101,843	97,959	909,313
Construction in progress.....	28,896	40,405	258,000
	1,368,677	1,326,076	12,220,330
Accumulated depreciation	(1,043,361)	(1,012,794)	(9,315,723)
Total property, plant and equipment	325,316	313,282	2,904,607
Intangible assets (Note 7):	4,806	5,320	42,911
Investments and other assets:			
Investment securities (Notes 3, 4 and 7)	82,706	69,045	738,446
Deferred tax assets (Note 8)	10,879	14,250	97,134
Other (Note 14)	11,120	8,473	99,286
Allowance for doubtful accounts	(80)	(102)	(714)
Total investments and other assets	104,625	91,666	934,152
Current assets:			
Cash and cash equivalents (Notes 3,4 and 7)	16,497	60,315	147,295
Receivables:			
Trade notes and accounts receivable (Note 3)	45,774	47,666	408,696
Allowance for doubtful accounts	(217)	(212)	(1,937)
Lease receivables and investment assets	8,567	8,077	76,491
Inventories (Note 5)	17,316	14,256	154,607
Deferred tax assets (Note 8)	3,222	5,010	28,768
Other (Notes 3 and 14)	7,025	9,838	62,723
Total current assets	98,184	144,950	876,643
Deferred charges	—	—	—
Total assets	¥532,931	¥555,218	\$4,758,313

See accompanying Notes to Consolidated Financial Statements.

Liabilities and Net Assets	Millions of yen		Thousands of U.S. dollars (Note 1)
	2017	2016	2017
Noncurrent liabilities:			
Long-term debt (Notes 3 and 7)	¥105,240	¥92,388	\$939,643
Provision for gas holder repairs	1,518	1,422	13,553
Reserve for safety measures	17,309	18,570	154,545
Deferred tax liabilities (Note 8)	953	905	8,509
Net defined benefit liability (Note 6)	15,946	26,200	142,375
Provision for gas appliance warranties	4,082	3,764	36,446
Other (Note 14)	8,079	7,758	72,134
Total noncurrent liabilities	153,127	151,007	1,367,205
Current liabilities:			
Short-term loans payable (Notes 3 and 7)	5,573	7,073	49,759
Current portion of noncurrent liabilities (Notes 3 and 7)	2,807	26,780	25,063
Trade notes and accounts payable (Note 3)	21,488	16,593	191,857
Income taxes payable	4,732	15,356	42,250
Other	38,402	53,223	342,875
Total current liabilities	73,002	119,025	651,804
Net assets (Notes 9 and 16):			
Shareholders' equity:			
Capital stock:			
Authorized - 805,998,157 shares			
Issued - 538,196,429 shares in 2017 and 541,276,429 shares in 2016	33,073	33,073	295,295
Capital surplus	8,387	8,387	74,884
Retained earnings	232,642	222,722	2,077,161
Less treasury stock -			
2,765,221 shares in 2017 and 68,729 shares in 2016	(2,232)	(51)	(19,929)
Total shareholders' equity	271,870	264,131	2,427,411
Accumulated other comprehensive income:			
Valuation difference on available-for-sale securities	38,214	32,481	341,196
Deferred (losses) gains on hedges	(444)	(4,213)	(3,964)
Foreign currency translation adjustments	2,868	3,009	25,607
Remeasurements of defined benefit plans	(5,706)	(10,222)	(50,946)
Total accumulated other comprehensive income	34,932	21,055	311,893
Total net assets	306,802	285,186	2,739,304
Total liabilities and net assets	¥532,931	¥555,218	\$4,758,313

Consolidated Statements of Income

TOHO GAS CO., LTD. and Consolidated Subsidiaries
Years ended March 31, 2017 and 2016

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2017	2016	2017
Net sales (Note 11)	¥390,434	¥479,870	\$3,486,018
Operating costs and expenses:			
Cost of sales	230,491	278,074	2,057,955
Selling, general and administrative expenses	136,754	141,071	1,221,018
	367,245	419,145	3,278,973
Operating income (Note 11)	23,189	60,725	207,045
Other income (expenses):			
Interest and dividend income	1,636	1,673	14,607
Interest expense	(1,010)	(1,551)	(9,018)
Loss on bond retirement	(675)	(937)	(6,027)
Other, net	1,350	1,222	12,054
	1,301	407	11,616
Net income before income taxes	24,490	61,132	218,661
Income taxes (Note 8):			
Current	6,745	18,406	60,223
Deferred	(4)	(283)	(35)
Total income taxes	6,741	18,123	60,188
Net income	17,749	43,009	158,473
Net income attributable to owners of the parent	¥17,749	¥43,009	\$158,473
Per share:	Yen		U.S. dollars
Net income attributable to owners of the parent	¥32.97	¥79.41	\$0.29
Cash dividends applicable to the year (Notes 2 and 16)	10.00	10.00	0.09

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Comprehensive Income

TOHO GAS CO., LTD. and Consolidated Subsidiaries
Years ended March 31, 2017 and 2016

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2017	2016	2017
Net income	¥17,749	¥43,009	\$158,473
Other comprehensive income (Note 10):			
Valuation difference on available-for-sale securities	5,733	(6,992)	51,187
Deferred gains (losses) on hedges	3,769	(15,710)	33,652
Foreign currency translation adjustments	(436)	223	(3,893)
Remeasurements of defined benefit plans	4,551	(9,697)	40,634
Share of other comprehensive income of entities accounted for using equity method	260	—	2,322
Total other comprehensive income	13,877	(32,176)	123,902
Comprehensive income	¥31,626	¥10,833	\$282,375
Comprehensive income attributable to:			
Owners of the parent	¥31,626	¥10,833	\$282,375
Non-controlling interests	—	—	—

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Changes in Net Assets

TOHO GAS CO., LTD. and Consolidated Subsidiaries
Years ended March 31, 2017 and 2016

	Number of shares of common stock	Millions of yen				
		Shareholders' equity				
		Capital stock	Capital surplus	Retained earnings	Treasury stock	Total shareholders' equity
Balance at March 31, 2015	545,966,429	¥33,073	¥8,388	¥188,522	(¥387)	¥229,596
Dividends from surplus				(5,432)		(5,432)
Net income attributable to owners of the parent				43,009		43,009
Purchase of treasury stock					(3,042)	(3,042)
Disposal of treasury stock			0		0	0
Retirement of treasury stock	(4,690,000)		(1)	(3,377)	3,378	
Change in scope of consolidation						
Net changes in items other than shareholders' equity						
Total changes in items during the period		—	(1)	34,200	336	34,535
Balance at March 31, 2016	541,276,429	¥33,073	¥8,387	¥222,722	(¥51)	¥264,131
Dividends from surplus				(5,396)		(5,396)
Net income attributable to owners of the parent				17,749		17,749
Purchase of treasury stock					(4,614)	(4,614)
Disposal of treasury stock				(0)	0	0
Retirement of treasury stock	(3,080,000)			(2,433)	2,433	—
Net changes in items other than shareholders' equity						
Total changes in items during the period		—	—	9,920	(2,181)	7,739
Balance at March 31, 2017	538,196,429	¥33,073	¥8,387	¥232,642	(¥2,232)	¥271,870

	Thousands of U.S. dollars (Note 1)				
	Shareholders' equity				
	Capital stock	Capital surplus	Retained earnings	Treasury stock	Total shareholders' equity
Balance at March 31, 2016	\$295,295	\$74,884	\$1,988,590	(\$456)	\$2,358,313
Dividends from surplus			(48,179)		(48,179)
Net income attributable to owners of the parent			158,473		158,473
Purchase of treasury stock				(41,196)	(41,196)
Disposal of treasury stock			(0)	0	0
Retirement of treasury stock			(21,723)	21,723	—
Net changes in items other than shareholders' equity					
Total changes in items during the period	—	—	88,571	(19,473)	69,098
Balance at March 31, 2017	\$295,295	\$74,884	\$2,077,161	(\$19,929)	\$2,427,411

See accompanying Notes to Consolidated Financial Statements.

	Millions of yen					
	Accumulated other comprehensive income					
	Valuation difference on available-for-sale securities	Deferred gains (losses) on hedges	Foreign currency translation adjustments	Remeasurements of defined benefit pension plan	Total accumulated other comprehensive income	Total net assets
Balance at March 31, 2015	¥39,473	¥11,497	¥2,786	(¥525)	¥53,231	¥282,827
Dividends from surplus						(5,432)
Net income attributable to owners of the parent ..						43,009
Purchase of treasury stock						(3,042)
Disposal of treasury stock						0
Retirement of treasury stock						
Change in scope of consolidation						
Net changes in items other than shareholders' equity ..	(6,992)	(15,710)	223	(9,697)	(32,176)	(32,176)
Total changes in items during the period	(6,992)	(15,710)	223	(9,697)	(32,176)	2,359
Balance at March 31, 2016	¥32,481	(¥4,213)	¥3,009	(¥10,222)	¥21,055	¥285,186
Dividends from surplus						(5,396)
Net income attributable to owners of the parent ..						17,749
Purchase of treasury stock						(4,614)
Disposal of treasury stock						0
Retirement of treasury stock						—
Net changes in items other than shareholders' equity ..	5,733	3,769	(141)	4,516	13,877	13,877
Total changes in items during the period	5,733	3,769	(141)	4,516	13,877	21,616
Balance at March 31, 2017	¥38,214	(¥444)	¥2,868	(¥5,706)	¥34,932	¥306,802

	Thousands of U.S. dollars (Note 1)					
	Accumulated other comprehensive income					Total net assets
	Valuation difference on available-for-sale securities	Deferred gains (losses) on hedges	Foreign currency translation adjustments	Remeasurements of defined benefit pension plan	Total accumulated other comprehensive income	
Balance at March 31, 2016	\$290,009	(\$37,616)	\$26,866	(\$91,268)	\$187,991	\$2,546,304
Dividends from surplus						(48,179)
Net income attributable to owners of the parent ..						158,473
Purchase of treasury stock						(41,196)
Disposal of treasury stock						0
Retirement of treasury stock						—
Net changes in items other than shareholders' equity ..	51,187	33,652	(1,259)	40,322	123,902	123,902
Total changes in items during the period	51,187	33,652	(1,259)	40,322	123,902	193,000
Balance at March 31, 2017	\$341,196	(\$3,964)	\$25,607	(\$50,946)	\$311,893	\$2,739,304

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

TOHO GAS CO., LTD. and Consolidated Subsidiaries
Years ended March 31, 2017 and 2016

	Millions of yen		Thousands of U.S. dollars (Note 1)
	2017	2016	2017
Cash flows from operating activities:			
Net income before income taxes	¥24,490	¥61,132	\$218,661
Adjustments for:			
Depreciation and amortization	35,482	32,987	\$316,803
Increase in net defined benefit liability and other allowances	(864)	5,280	(\$7,714)
Interest and dividend income	(1,636)	(1,673)	(\$14,607)
Interest expense	1,010	1,551	\$9,018
Decrease in trade notes and accounts receivable	1,892	13,365	\$16,893
Increase (decrease) in inventories	(3,060)	14,042	(\$27,321)
Increase in trade notes and accounts payable	4,893	624	\$43,687
Other	(8,054)	895	(\$71,911)
	54,153	128,203	\$483,509
Interests and dividends received	1,636	1,673	\$14,607
Interests paid	(1,060)	(1,577)	(\$9,464)
Income taxes paid	(17,465)	(13,375)	(\$155,938)
Net cash provided by operating activities	37,264	114,924	\$332,714
Cash flows from investment activities:			
Purchases of investment securities	(5,840)	(200)	(52,143)
Proceeds from sale of investment securities	185	25	1,652
Purchases of noncurrent assets	(49,298)	(40,101)	(440,161)
Proceeds from sale of noncurrent assets	11	107	98
Other	(3,026)	(2,027)	(27,017)
Net cash used in investment activities	(57,968)	(42,196)	(517,571)
Cash flows from financing activities:			
Net (decrease) in short-term bank loans	(1,500)	(4,949)	(13,393)
Proceeds from long-term loans payable	15,605	10,736	139,330
Repayment of long-term loans payable	(16,717)	(8,176)	(149,259)
Proceeds from issuance from bonds	9,939	—	88,741
Redemption of bonds	(20,673)	(20,935)	(184,580)
Purchase of treasury stock	(4,614)	(3,042)	(41,196)
Cash dividends paid	(5,396)	(5,435)	(48,179)
Other	394	(16)	3,518
Net cash used in financing activities	(22,962)	(31,817)	(205,018)
Effect of exchange rate change on cash and cash equivalents	(152)	(19)	(1,357)
Net increase in cash and cash equivalents	(43,818)	40,892	(391,232)
Cash and cash equivalents at beginning of year	60,315	19,423	538,527
Cash and cash equivalents at end of year	¥16,497	¥60,315	147,295

See accompanying Notes to Consolidated Financial Statements.

Notes to Consolidated Financial Statements

TOHO GAS CO., LTD. and Consolidated Subsidiaries

1 Basis of presenting consolidated financial statements

The accompanying consolidated financial statements of TOHO GAS CO., LTD. (the "Company") and its consolidated subsidiaries (together with the Company, the "TOHO GAS Group") have been prepared in accordance with the provisions set forth in the Japanese Financial Instruments and Exchange Law and its related accounting regulations and in conformity with accounting principles generally accepted in Japan ("Japanese GAAP"), which are different in certain respects as to application and disclosure requirements from International Financial Reporting Standards. The Company, as a regulated company, also complies with the GAS Business Law and its related accounting regulations for preparing the financial statements.

The accompanying consolidated financial statements have been restructured and translated into English from the consolidated

financial statements of the Company prepared in accordance with Japanese GAAP and filed with the appropriate Local Finance Bureau of the Ministry of Finance as required by the Financial Instruments and Exchange Law. Certain supplementary information included in the statutory Japanese language consolidated financial statements, but not required for fair presentation, is not presented in the accompanying consolidated financial statements.

The translation of the Japanese yen amounts into U.S. dollar amounts is included solely for the convenience of readers outside Japan, using the prevailing approximate exchange rate at March 31, 2017, which was ¥112 to U.S. \$1.00. The translations should not be construed as representations that the Japanese yen amounts have been, could have been or could in the future be converted into U.S. dollars at this or any other rate of exchange.

2 Summary of significant accounting policies

Consolidation

The consolidated financial statements include the accounts of the Company and its consolidated subsidiaries (22 in 2017 and 2016). All significant intercompany transactions and accounts are eliminated in consolidation. The difference between the cost of investments in consolidated subsidiaries and the underlying equity in the net assets adjusted based on the fair value at the time of acquisition is charged to income as incurred.

MEET Europe Natural Gas, Lda. was newly established and has become an equity method affiliate from the current fiscal year.

Though the fiscal year-end of certain consolidated subsidiaries differ from the consolidated fiscal year-end of the Company, the Company has consolidated the subsidiaries' financial statements as of their respective year-end. Significant transactions for the period between a subsidiary's year-end and the Company's year-end are adjusted for on consolidation.

Property, plant and equipment

Depreciation of property, plant and equipment is computed mainly by the declining balance method over the estimated useful life of the asset. However, buildings (excluding facilities attached to buildings), which were acquired since April 1, 1998 and facilities attached to buildings and structures, which were acquired since April 1, 2016 are depreciated by the straight-line method.

Property, plant, and equipment that are capitalized under finance lease arrangements and that do not transfer ownership of the leased asset to the lessee are depreciated using the straight-line method over the term of the lease with the assumption of no residual value.

Investments

The TOHO GAS Group classifies certain investments in debt and equity securities as "held-to-maturity," "trading" or "available-for-sale." The classification determines the respective accounting method as stipulated by the accounting standard for financial instruments. Investments in debt securities that are classified as held-to-maturity are carried at amortized cost. Available-for-sale securities with available market quotations are stated at fair value, and net unrealized gain or loss on these securities is reported as a separate component of net assets or shareholders' equity, net of applicable income taxes. Available-for-sale securities without available market quotations are carried at cost determined by the moving average method. Adjustments in carrying values from write-downs are charged to

income when a decline in value is deemed other than temporary.

Inventories

Inventories are mostly stated at the moving average cost (balance sheet prices are calculated using the book value reduction method based on any reduction in profitability).

Deferred charges

Bond issue costs are charged to income as incurred.

Allowance for doubtful accounts

An allowance for doubtful accounts has been provided for at the aggregate amount of estimated credit loss based on an individual financial review of certain doubtful or troubled receivables and a general reserve for other receivables based on the historical loss experience of a certain past period.

Provision for gas holder repairs

The TOHO GAS Group provides for future repairs of gas holders by estimating future expenditures and charging them to income in equal annual amounts over the period to the next repair.

Provision for safety measures

The TOHO GAS Group provides an allowance for replacement of pipelines by estimating future expenditures and charging them to income to replace the aged white galvanized branch pipes, pipes buried under the roads that are important in terms of disaster prevention, and pipes connected with important buildings for security reasons.

Provision for gas appliance warranties

The TOHO GAS Group provides an allowance for gas appliance warranties by estimating future expenditures and charging them to income to provide the warranty service, etc.

Employees' retirement benefits

In the calculation of retirement benefit obligations, the expected retirement benefits are attributed to the period up to the end of the current fiscal year based on a benefit formula basis. Unrecognized actuarial differences from those which were assumed and from changes in the assumptions themselves are amortized on a straight-line basis over ten years, which is within the average remaining service years of employees, from the year following the year in which they arise.

Translation of foreign currency accounts

Receivables, payables and securities, other than stocks of subsidiaries and certain other securities, are translated into Japanese yen at the exchange rates prevailing at the fiscal year-end. Transactions in foreign currencies are recorded based on the prevailing exchange rates on the transaction date. Resulting translation gains and losses are included in net asset.

Derivatives

Derivatives are valued at fair value when hedge accounting is not appropriate or when there is no hedging designation, and the gains and losses on the derivatives are recognized in current earnings. Certain transactions classified as hedging transactions such as commodity swaps, foreign exchange forward contracts and interest rate swaps are accounted for under a deferral method in which unrealized gains and losses on the hedging instruments are carried as net assets on the balance sheets until the gain or loss on the related hedged item is realized. According to the special treatment permitted by the accounting standards for financial instruments, hedging interest rate swaps are accounted for on an accrual basis and recorded net of interest expense generated from the hedged borrowings if certain conditions are met.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, readily-available deposits and short-term highly liquid debt investments with original maturities of three months or less.

Income taxes

Income taxes are accounted for by the asset liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carryforwards. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date.

Research and development expenses

Research and development expenses are charged to income as incurred. In the accompanying consolidated statements of income, research and development expenses included in cost of sales and selling, general and administrative expenses amounted to ¥1,876 million (\$16,750 thousand) and ¥2,156 million for the years ended March 31, 2017 and 2016, respectively.

Appropriation of surplus

Cash dividends are recorded in the fiscal year when the proposed appropriation of surplus is approved by the Board of Directors and/or shareholders.

Amounts per share

Net income per share is computed by dividing income available to shareholders by the weighted average number of shares of common stock outstanding during the respective year. Diluted net income per share is not disclosed as the Company had no dilutive common shares for the years ended March 31, 2017 or 2016.

Cash dividends per share applicable to the year are dividends declared by the Company applicable to the respective year and include dividends approved or to be approved after the balance sheet date.

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year's presentation.

Change in accounting policy

The TOHO GAS Group has adopted "Revised Accounting Standard for Business Combinations" (ASBJ Statement No. 21, September 13, 2013 (hereinafter, "Statement No. 21")), "Revised Accounting Standard for Consolidated Financial Statements" (ASBJ Statement No. 22, September 13, 2013 (hereinafter, "Statement No. 22")) and "Revised Accounting Standard for Business Divestitures" (ASBJ Statement No. 7, September 13, 2013 (hereinafter, "Statement No. 7")) (together, the "Business Combination Accounting Standards"), from the previous fiscal year ended March 31, 2016. As a result, the Company changed its accounting policies to recognize in capital surplus the differences arising from the changes in the Company's ownership interest of subsidiaries over which the Company continues to maintain control and to record acquisition related costs as expenses in the fiscal year in which the costs are incurred. In addition, the Company changed its accounting policy for the reallocation of acquisition costs due to the completion following provisional accounting to reflect such reallocation in the consolidated financial statements for the fiscal year in which the business combination took place. The Company also changed the presentation of net income.

With regard to the application of the Business Combination Accounting Standards, the Company followed the provisional treatments in article 58-2 (4) of Statement No. 21, article 44-5 (4) of Statement No. 22 and article 57-4 (4) of Statement No. 7 with application from the beginning of the previous fiscal year prospectively.

In the consolidated statement of cash flows, cash flows from acquisition or disposal of shares of subsidiaries with no changes in the scope of consolidation are included in "Cash flows from financing activities" and cash flows from acquisition related costs for shares of subsidiaries with changes in the scope of consolidation or costs related to acquisition or disposal of shares of subsidiaries with no changes in the scope of consolidation are included in "Cash flows from operating activities".

There was no effect on the consolidated financial statements or per share information of the previous fiscal year.

Due to amendments to the Japanese Corporation Tax Act, the TOHO GAS Group has adopted "Practical Solution on a change in depreciation method due to Tax Reform 2016" (Practice Issue Task Force No.32, June 17, 2016) from the current fiscal year ended March 31, 2017 and has changed the depreciation method for buildings, facilities attached to buildings and structures, which were acquired since April 1, 2016, from the declining balance method to the straight-line method.

As a result, operating income and income before income taxes for the current fiscal year ended March 31, 2017 increased by ¥1,265 million (\$11,295 thousand).

(Additional information)

The TOHO GAS Group has adopted "Revised Implementation Guidance on Recoverability of Deferred Tax Assets" (ASBJ Guidance No. 26, March 28, 2016) from the current fiscal year.

3 Fair values of financial instruments

1. Qualitative information on financial instruments

① Policies for using financial instruments

The TOHO GAS Group invests its excess cash in bank deposits and other safe financial instruments. Cash needed for operations and other business activities is acquired through the issuance of corporate bonds and commercial paper through financing from banks and other financial institutions.

② Details of financial instruments used and exposure to risks and how they arise

Trade notes and accounts receivable, which are operational credit, are exposed to customers' credit risk. Securities and investment securities comprise mainly equity securities of corporations with which the Company has business relations. These securities are exposed to the risk of market price fluctuations.

The due dates for most trade notes and accounts payable, which are operational debt, are within one year. Corporate bonds and loans payable are used to procure working capital and cash for capital investments. The longest redemption date is 29 years after the end of the current fiscal year. Long-term loans payable with variable interest rates are exposed to the risk of interest rate fluctuations. Variable interest rates on some of these liabilities mainly interest rate swap contracts, are hedged by derivative contracts.

The TOHO GAS Group uses commodity swaps, foreign exchange forward contracts and interest rate swaps only for the purpose of mitigating the risk of fluctuations in market prices of raw materials and interest rates. The TOHO GAS Group does not use derivatives for speculative trading purposes. The derivatives are executed with creditworthy financial institutions, and the Company's management believes there is little risk of default by the counterparties.

③ Policies and processes for managing risk

1) Management of credit risk

As for trade receivables, the TOHO GAS Group monitors the status of major customers in accordance with its risk

management rules by monitoring the due dates and balances of receivables of individual customers, quickly identifying any deterioration in the financial position of customers and reducing the uncollectability of receivables. When derivative contracts are used, the TOHO GAS Group enters into derivative contracts only with highly rated financial institutions in order to reduce the credit risk of counterparty default.

2) Management of market risk

To hedge the risk of fluctuation in the purchase price of raw materials and interest rates, the Company uses commodity swap contracts, foreign exchange forward contracts and interest swap contracts to stabilize the cash flow of the hedged transactions and avoid or mitigate the impact of market price fluctuations. Market prices of investment securities are monitored on a quarterly basis.

Derivative transactions are executed and managed by the Company in accordance with its in-house regulations stipulating approval authority, management and reporting methods and other matters regarding derivative transactions. To ensure an effective cross-checking function, derivative transactions are administered and risk managed by a department separate from the department responsible for the execution of the relevant transactions.

3) Management of liquidity risk in funding

The liquidity risk of the TOHO GAS Group is managed by preparing and updating a cash management plan.

④ Supplemental information on fair values

The current price of a financial product is based on its market price or a price calculated using an alternative method if the product does not have an available market price. Since the calculation of the current price reflects variable factors, the current price may vary if different factors and assumptions are used for the calculation. Contract prices of derivative contracts or other amounts indicated in the table below, do not necessarily reflect the market risk of the derivative contracts themselves.

Carrying values and fair values of the financial instruments included in the consolidated balance sheets at March 31, 2017 and 2016 were as follows:

	Millions of yen		
	Carrying value	Fair value	Difference
For 2017:			
Assets:			
Cash and time deposits	¥16,576	¥16,576	¥ —
Trade notes and accounts receivable	45,774	45,774	—
Securities and investment securities	70,502	70,502	—
Total	132,852	132,852	—
Liabilities:			
Trade notes and accounts payable	21,488	21,488	—
Short-term loans payable	5,573	5,573	—
Bonds payable, including current portion	70,000	72,074	2,074
Long-term loans payable, including current portion	37,971	38,448	477
Total	135,032	137,583	2,551
Derivative transactions	(616)	(616)	—
For 2016:			
Assets:			
Cash and time deposits	¥25,393	¥25,393	¥ —
Trade notes and accounts receivable	47,666	47,666	—
Securities and investment securities	97,764	97,764	—
Total	170,823	170,823	—
Liabilities:			
Trade notes and accounts payable	16,593	16,593	—
Short-term loans payable	7,073	7,073	—
Bonds payable, including current portion	79,998	84,340	4,342
Long-term loans payable, including current portion	39,106	39,935	829
Total	142,770	147,941	5,171
Derivative transactions	(5,843)	(5,843)	—
	Thousands of U.S. dollars		
	Carrying value	Fair value	Difference
For 2017:			
Assets:			
Cash and time deposits	\$148,000	\$148,000	\$ —
Trade notes and accounts receivable	408,696	408,696	—
Securities and investment securities	629,482	629,482	—
Total	1,186,178	1,186,178	—
Liabilities:			
Trade notes and accounts payable	191,857	191,857	—
Short-term loans payable	49,759	49,759	—
Bonds payable, including current portion	625,000	643,518	18,518
Long-term loans payable, including current portion	339,027	343,286	4,259
Total	1,205,643	1,228,420	22,777
Derivative transactions	(5,500)	(5,500)	—

Note: The calculation methods for fair value of financial instruments

1. Assets

(1) Cash and time deposits, trade notes and accounts receivable
Since these items are settled in a short period of time, their fair value is approximate to the carrying value. Accordingly, the carrying value is used as the fair value.

(2) Securities and investment securities

The fair value of the Company's equity securities is based on the prices quoted on the stock exchange. The fair value of other investment securities is based on the price quoted by financial institutions or the published reference price.

2. Liabilities

(1) Trade notes and accounts payable and short-term loans payable
Since these items are settled in a short period of time, their fair value is approximate to the carrying value. Accordingly, the carrying value is used as the fair value.

(2) Bonds payable

The fair value of corporate bonds issued by the Company is calculated by the market price.

(3) Long-term debt

The fair value of these accounts is calculated by the sum of the principal and interest discounted by the interest rate applicable to a similar new loan or transaction. "Special accounting treatment for interest rate swap contracts" applies to some long-term loans with variable interest rates. Current prices of such loans are calculated by the sum of the principal and interest treated as a unit together with the relevant interest rate swap contract and discounted by the interest rate reasonably estimated to apply to a similar loan.

Financial instruments whose fair value cannot be reliably determined were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Nonmarketable securities			
Unlisted equity securities	¥4,570	¥4,631	\$40,803
Investments in affiliates	7,634	1,650	\$68,161

A maturity analysis for cash and time deposits, trade notes and accounts receivable and securities and investment securities is as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
	Due within one year	Due within one year	Due within one year
Cash and time deposits	¥16,576	¥25,393	\$148,000
Trade notes and accounts receivable	45,774	47,666	408,696
Securities and investment securities	—	35,000	—
	¥62,350	¥108,059	\$556,696

A maturity analysis for short-term bank loans payable, bonds payable and long-term bank loans payable is as follows:

	Millions of yen					
	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
For 2017:						
Short-term bank loans payable.....	¥5,573	¥ —	¥ —	¥ —	¥ —	¥ —
Bonds payable	—	10,000	10,000	—	—	50,000
Long-term bank loans payable	2,731	13,558	3,446	2,629	671	14,936
	¥8,304	¥23,558	¥13,446	¥2,629	¥671	¥64,936
For 2016:						
Short-term bank loans payable.....	¥7,073	¥ —	¥ —	¥ —	¥ —	¥ —
Bonds payable.....	10,000	5,000	10,000	10,000	—	45,000
Long-term bank loans payable	16,716	2,607	4,479	3,328	2,503	9,473
	¥33,789	¥7,607	¥14,479	¥13,328	¥2,503	¥54,473
	Thousands of U.S. dollars					
	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
For 2017:						
Short-term bank loans payable.....	\$49,759	\$ —	\$ —	\$ —	\$ —	\$ —
Bonds payable	—	89,286	89,286	—	—	446,428
Long-term bank loans payable	24,384	121,053	30,768	23,473	5,992	133,357
	\$74,143	\$210,339	\$120,054	23,473	\$5,992	\$579,785

4 Securities and investments

In accordance with the accounting standard for financial instruments, investment securities include equity securities, bonds and other of which the aggregate cost, gross unrealized gains/losses and fair value pertaining to available-for-sale securities at March 31, 2017 and 2016 were as follows.

Available-for-sale securities

Securities with fair and carrying value exceeding cost:

	Millions of yen			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair and carrying value
March 31, 2017				
Equity securities	¥17,436	¥51,887	¥ —	¥69,323
Other	5	7	—	12
	¥17,441	¥51,894	¥ —	¥69,335
March 31, 2016				
Equity securities	¥15,833	¥44,513	¥ —	¥60,346
Other	5	7	—	12
	¥15,838	¥44,520	¥ —	¥60,358
	Thousands of U.S. dollars			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair and carrying value
March 31, 2017				
Equity securities	\$155,678	\$463,277	\$ —	\$618,955
Other	45	62	—	107
	\$155,723	\$463,339	\$ —	\$619,062

Securities with fair and carrying value not exceeding cost:

	Millions of yen			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair and carrying value
March 31, 2017				
Equity securities	¥1,262	¥ —	(¥95)	¥1,167
	¥1,262	¥ —	(¥95)	¥1,167
March 31, 2016				
Equity securities	¥2,864	¥ —	(¥458)	¥2,406
Other	35,000	—	—	35,000
	¥37,864	¥ —	(¥458)	¥37,406
	Thousands of U.S. dollars			
	Cost	Gross unrealized gains	Gross unrealized losses	Fair and carrying value
March 31, 2017				
Equity securities	\$11,268	\$ —	(\$848)	\$10,420
	\$11,268	\$ —	(\$848)	\$10,420

Total sales of available-for-sale securities for the years ended March 31, 2017 and 2016 amounted to ¥186 million (\$1,660 thousand) and ¥25 million, respectively. The related gains for the years ended March 31, 2017 and 2016 amounted to ¥56 million (\$500 thousand) and ¥12 million, respectively.

5 Inventories

Inventories at March 31, 2017 and 2016 consisted of the following:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Finished products	¥4,321	¥3,547	\$38,580
Work-in-process	715	630	6,384
Raw materials and supplies	12,280	10,079	109,643
	¥17,316	¥14,256	\$154,607

6 Employees' retirement benefits liability

The TOHO GAS Group principally has a defined benefit pension plan and a lump-sum retirement benefit plan which substantially cover all employees. Projected benefit obligation of certain subsidiaries was calculated using the simplified calculation method as permitted by the accounting standard for employee retirement benefits. The Company has established a retirement benefit trust for its lump-sum retirement benefit plan and corporate pension plan.

Reconciliation of the beginning and ending balances for retirement benefit obligations at March 31, 2017 and 2016 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Beginning balance of the retirement benefit obligation	¥120,162	¥108,308	\$1,072,875
Service cost	3,543	2,956	31,634
Interest cost	237	958	2,116
Accruals of actuarial gains and losses	(3,344)	12,367	(29,857)
Payment of retirement benefits	(4,439)	(4,427)	(39,634)
Ending balance of the retirement benefit obligation	¥116,159	¥120,162	\$1,037,134

Note: Including a system for the application of the simplified method

Reconciliation of the beginning and ending balances for pension plan assets was as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Fair value of pension plan assets at beginning of year	¥93,962	¥86,526	\$838,946
Expected return on pension plan assets	1,879	1,731	16,777
Accruals of actuarial gains and losses	377	(1,438)	3,366
Contributions from the employer	3,461	3,478	30,902
Lump-sum retirement benefit plan	4,000	7,000	35,714
Payment of retirement benefits	(3,466)	(3,335)	(30,946)
Fair value of pension plan assets at ending of year	¥100,213	¥93,962	\$894,759

Reconciliation of the retirement benefit obligation and fair value of pension plan assets at the end of year, net defined benefit liability and the fair valued pension plan assets were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Projected benefit obligation of funded plans	¥111,571	¥115,714	\$996,170
Fair value of pension plan assets	(100,213)	(93,962)	(894,759)
	11,358	21,752	101,411
Projected benefit obligation of unfunded obligation	4,588	4,448	40,964
Net of assets and liabilities	15,946	26,200	142,375
Net defined benefit liability	15,946	26,200	142,375
Net defined benefit assets	—	—	—
Net of assets and liabilities	¥15,946	¥26,200	\$142,375

Note1: Including a system for the application of the simplified method

Note2: Because a retirement benefit trust was established for the lump-sum retirement benefit plans, the projected benefit obligation of funded plans include lump-sum payment plans. Similarly, pension assets include a retirement benefit trust.

Retirement benefit expense and amount of the detailed items

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Components of net periodic retirement benefit expense:			
Service cost	¥3,543	¥2,956	\$31,634
Interest cost	237	958	2,116
Expected return on pension plan assets	(1,879)	(1,731)	(16,777)
Recognized actuarial differences	2,582	382	23,054
Net periodic retirement benefit expense related to defined benefit pension plan	¥4,483	¥2,565	\$40,027

Remeasurements of defined benefit plans included in other comprehensive income (before tax effects) at March 31, 2017 and 2016 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Actuarial differences	¥6,303	(¥13,423)	\$56,277

Total remeasurement of defined benefit pension plan included in other comprehensive income (before tax effects) at March 31, 2017 and 2016 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Actuarial differences	(¥7,854)	(¥14,157)	(\$70,125)

Plan assets

	2017	2016
Bond	58%	57%
Equity securities	22%	18%
General account	16%	17%
Other	4%	8%
Total	100%	100%

For the fiscal year ended March 31, 2017 and 2016, assets in the retirement benefit trust, which was established for the lump-sum payment plans accounted for 11% and 7% of the total pension plan assets.

To determine the expected long-term rate of return on pension plan assets, we considered the composition of plan assets and the expected current return, and the rate of return on long-term expected current and future assets from a variety of assets that make up the plan assets.

Major assumptions used in the calculations above for the years ended March 31, 2017 and 2016 were as follows:

	2017	2016
Discount rate	0.4%	0.2%
Expected long-term rate of return on pension plan assets	2.0%	2.0%

7 Bank loans and long-term debt

Short-term bank loans consisted of short-term notes payable bearing interest at an annual average rate of 0.5% at March 31, 2017.

Long-term debt and other interest-bearing liabilities at March 31, 2017 and 2016 comprised the following:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Domestic unsecured notes due 2018 at a rate of 3.175%	¥ —	¥5,000	\$ —
Domestic unsecured notes due 2023 at a rate of 1.12%	10,000	10,000	89,286
Domestic unsecured notes due 2016 at a rate of 2.07%	—	10,000	0
Domestic unsecured notes due 2022 at a rate of 2.06%	—	4,998	0
Domestic unsecured notes due 2018 at a rate of 1.658%	10,000	10,000	89,286
Domestic unsecured notes due 2027 at a rate of 1.628%	10,000	10,000	89,285
Domestic unsecured notes due 2022 at a rate of 0.792%	10,000	10,000	89,286
Domestic unsecured notes due 2023 at a rate of 0.933%	10,000	10,000	89,285
Domestic unsecured notes due 2019 at a rate of 0.28%	10,000	10,000	89,286
Domestic unsecured notes due 2046 at a rate of 0.804%	10,000	—	89,286
Loans from banks, insurance companies and government agencies due through 2031 at interest rates ranging from 0.10% to 3.07% per annum at March 31, 2017	37,971	39,106	339,027
Capitalized lease obligations	960	979	8,571
Others	—	—	—
	108,931	120,083	972,598
Less amounts due within one year	(2,804)	(26,777)	(25,036)
	¥106,127	¥93,306	\$947,562

The Company entered into debt assumption agreements for 3.175% notes payable due in 2018 in the amount of 10,000 million and 2.06% notes payable due in 2022 in the amount of 10,000 million, and treated the bonds as having been redeemed. The Company remains contingently liable on the bond redemption obligation.

Assets pledged as collateral mainly for trade accounts payable and long-term debt in the aggregate amounts of ¥25 million (\$219 thousand) and ¥25 million at March 31, 2017 and 2016, respectively, were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Other facilities	¥16	¥16	\$143
Construction in progress	6,866	5,727	61,304
Intangible assets	2,365	2,446	21,116
Investment securities	1,121	1,054	10,009
Cash and deposits	319	685	2,848
Other	5,541	3,507	49,473
	¥16,228	¥13,435	\$144,893

The annual maturities of long-term debt and other interest bearing liabilities at March 31, 2017 were as follows:

Year ending March 31,	Millions of yen	Thousands of U.S. dollars
2017	¥2,804	\$25,036
2018	23,625	210,937
2019	13,512	120,643
2020	2,694	24,054
2021	736	6,571
2022 and thereafter	65,560	585,357
	¥108,931	\$972,598

8 Income tax

Income taxes of the TOHO GAS Group consist of corporate income taxes, inhabitants taxes and enterprise taxes. Enterprise taxes for the gas business are included in selling, general and administrative expenses in the accompanying consolidated statements of income.

Components of deferred tax assets and liabilities at March 31, 2017 and 2016 were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Deferred tax assets:			
Net defined benefit liability	¥7,808	¥9,433	\$69,714
Depreciation	5,631	5,223	50,276
Reserve for safety measures	4,819	5,149	43,027
Prepaid expenses	1,937	1,822	17,295
Other	10,409	12,780	92,938
Less valuation allowance	(1,977)	(1,981)	(17,652)
	28,627	32,426	\$255,598
Deferred tax liabilities:			
Unrealized gains on available-for-sale securities	(13,585)	(11,582)	(121,294)
Reserve for overseas investment loss	(1,178)	(859)	(10,518)
Deferred gains on hedges	(585)	(1,453)	(5,223)
Deferred capital gains	(131)	(134)	(1,170)
Other	0	(43)	0
	(15,479)	(14,071)	(138,205)
Net deferred tax assets	¥ 13,148	¥ 18,355	\$ 117,393

For the fiscal year ended March 31, 2017 and 2016, the disclosure was omitted because the difference between the tax rate after application of tax effect accounting and the statutory tax rate was below 5% of the statutory tax rate.

9 Net assets

Under the Japanese Corporate Law ("the Law"), the entire amount paid for new shares is required to be designated as capital stock. However, a company may, by a resolution of the Board of Directors, designate an amount not exceeding one half of the price of the new shares as additional paid-in capital, which is included in capital surplus.

Under the Law, in cases in which a dividend distribution of surplus is made, the smaller of an amount equal to 10% of the dividend or the excess, if any, of 25% of capital stock over the total of additional paid-in capital and legal earnings reserve must be set aside as additional paid-in capital or legal earnings reserve. Legal earnings reserve is included in retained earnings in the accompanying consolidated balance sheets. Under the Law, legal earnings reserve and additional paid-in capital can be used to eliminate or reduce a deficit by a resolution of the shareholders' meeting.

Additional paid-in capital and legal earnings reserve may not be distributed as dividends. All additional paid-in capital and all legal earnings reserve may be transferred to other capital surplus and retained earnings, respectively, which are potentially available for dividends. At March 31, 2017 and 2016, respectively, capital surplus consisted principally of additional paid-in capital. In addition, retained earnings included legal earnings reserve in the amount of ¥8,780 million (\$78,393 thousand) at both March 31, 2017 and 2016.

The maximum amount that the Company can distribute as dividends is calculated based on the nonconsolidated financial statements of the Company in accordance with Japanese laws.

During the year ended March 31, 2017, the Company retired 3,080,000 shares of the treasury stock through a reduction of retained earnings. As a result, the number of issued shares of common stock decreased from 541,276,429 shares to 538,196,429 shares for the year ended March 31, 2017.

In November 2016, the Company paid interim dividends of ¥2,691 million (\$24,027 thousand), ¥5.0 per share. For year-end dividends, see Note 16.

10 Statements of comprehensive income

The amount of reclassification adjustments and the tax effects concerning other comprehensive income, at March 31, 2017 and 2016 were as follows :

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Net changes in valuation difference on available-for-sale securities			
Increase (decrease) during the year	¥7,789	(¥10,164)	\$69,544
Reclassification adjustments	(52)	72	(464)
Subtotal before tax	7,737	(10,092)	69,080
Tax benefit or (expense)	(2,004)	3,100	(17,893)
Subtotal net of tax	5,733	(6,992)	51,187
Net changes in deferred (losses) gains on hedges			
Increase (decrease) during the year	2,012	(15,318)	17,964
Reclassification adjustments	3,152	(6,599)	28,143
Adjustments for amounts transferred to initial carrying amount of hedged items	63	(5)	563
Subtotal before tax	5,227	(21,922)	46,670
Tax benefit or (expense)	(1,458)	6,212	(13,018)
Subtotal net of tax	3,769	(15,710)	33,652
Net changes in foreign currency translation adjustments			
Decrease (increase) during the year	(436)	223	(3,893)
Subtotal net of tax	(436)	223	(3,893)
Net changes in remeasurements of defined benefit plans			
Increase (decrease) during the year	3,721	(13,805)	33,223
Reclassification adjustments	2,582	382	23,054
Subtotal before tax	6,303	(13,423)	56,277
Tax benefit or (expense)	(1,752)	3,726	(15,643)
Subtotal net of tax	4,551	(9,697)	40,634
Net changes in share of other comprehensive income of entities accounted for using equity method			
Increase (decrease) during the year	260	—	2,322
Subtotal net of tax	260	—	2,322
Total other comprehensive income	13,877	(32,176)	123,902

11 Segment information

1. General information about reportable segments

The TOHO GAS Group defines reportable segments as constituent business units of the TOHO GAS Group for which discrete financial information is available and reviewed regularly by the Board of Directors to determine the best allocation of managerial resources and to evaluate business performance. The three reportable segments of the TOHO GAS Group are "Gas Sales", "Gas Appliance Sales and Related Construction" and "LPG and Other Energies." They are determined based on the GAS Business Law and its related accounting regulations.

The main products and services of each reporting segment are as follows:

Gas Sales: Products, supplies and sales of gas

Gas Appliance Sales and Related Construction: Gas appliance sales and related construction

LPG and Other Energies: LPG sales, LPG appliance sales, LNG sales, Electricity business, District heating and cooling, and sales of coke and petroleum products

2. Basis of measurement for reported segment income or loss, segment assets and other material items

The accounting methods for the reporting segments are consistent with the accounting methods described in Note 2, "Summary of significant accounting policies". Intersegment sales and transfers are attributable to transactions among group companies and calculated based on market value.

3. Information for reported segment income or loss, segment assets and other material items

Information for reported segments as of and for the years ended March 31, 2017 and 2016 was as follows:

	Millions of yen							
	Reported segments			Total	Other (Note 1)	Total	Adjustments (Note 2)	Consolidated (Note 3)
	Gas Sales	Gas Appliance Sales and Related Construction	LPG and Other Energies					
For 2017:								
Net sales:								
External customers	¥268,684	¥35,025	¥65,689	¥369,398	¥21,036	¥390,434	¥ —	¥390,434
Intersegment	64	1,836	768	2,668	16,511	19,179	(19,179)	—
Total net sales	268,748	36,861	66,457	372,066	37,547	409,613	(19,179)	390,434
Segment income (loss)	¥18,795	(¥169)	¥1,534	¥20,160	¥1,737	¥21,897	¥1,292	¥23,189
Segment assets	¥342,424	¥14,496	¥45,470	¥402,390	¥71,415	¥473,805	¥59,126	¥532,931
Other items:								
Depreciation expenses	31,758	166	2,253	34,177	1,366	35,543	(61)	35,482
Investment in entities accounted for using equity method	—	—	—	—	—	—	5,730	5,730
Capital expenditures	39,483	133	5,685	45,301	2,917	48,218	(69)	48,149
For 2016:								
Net sales:								
External customers	¥354,970	¥34,704	¥67,944	¥457,618	¥22,252	¥479,870	¥ —	¥479,870
Intersegment	78	3,089	721	3,888	16,659	20,547	(20,547)	—
Total net sales	355,048	37,793	68,665	461,506	38,911	500,417	(20,547)	479,870
Segment income (loss)	¥55,862	¥65	¥1,970	¥57,897	¥1,604	¥59,501	¥1,224	¥60,725
Segment assets	¥380,787	¥17,190	¥40,668	¥438,645	¥72,212	¥510,857	¥44,361	¥555,218
Other items:								
Depreciation expenses	29,808	150	2,154	32,112	953	33,065	(78)	32,987
Capital expenditures	34,649	233	2,784	37,666	5,461	43,127	117	43,244

	Thousands of U.S. dollars							
	Reported segments			Total	Other (Note 1)	Total	Adjustments (Note 2)	Consolidated (Note 3)
	Gas Sales	Gas Appliance Sales and Related Construction	LPG and Other Energies					
For 2017:								
Net sales:								
External customers	\$2,398,964	\$312,723	\$586,509	\$3,298,196	\$187,822	\$3,486,018	\$ —	\$3,486,018
Intersegment	572	16,393	6,857	23,822	147,419	171,241	(171,241)	—
Total net sales	2,399,536	329,116	593,366	3,322,018	335,241	3,657,259	(171,241)	3,486,018
Segment income (loss)	\$167,813	(\$1,509)	\$13,696	\$180,000	\$15,509	\$195,509	\$11,536	\$207,045
Segment assets	\$3,057,357	\$129,429	\$405,982	\$3,592,768	\$637,634	\$4,230,402	\$527,911	\$4,758,313
Other items:								
Depreciation expenses	283,554	1,482	20,116	305,152	12,196	317,348	(545)	316,803
Investment in entities accounted for using equity method	—	—	—	—	—	—	51,161	51,161
Capital expenditures	352,526	1,188	50,759	404,473	26,045	430,518	(616)	429,902

Notes: 1. The "Other" segment incorporates operations not included in reported segment, including LNG processing under contract, leasing of buildings, engineering of gas production plants, comprehensive utility service business, sales of housing equipment, data processing services, and other leasing and other business.

2. The "Adjustments" column in "Segment income" denotes eliminations of intersegment transactions. "Segment assets" in the "Adjustments" column denotes unallocated general corporate items which were not assigned to specific segments, such as long-term investments in securities.

3. Segment income in the table above is reconciled to operating income on the accompanying consolidated statements of income.

Enterprise-wide information for the year ended March 31, 2017 and 2016

(1) Information about products and services:

	Millions of yen			
	Gas Sales	LPG	Other	Total
For 2017:				
Net sales to external customers	¥268,684	¥46,166	¥75,584	¥390,434
	Millions of yen			
	Gas Sales	LPG	Other	Total
For 2016:				
Net sales to external customers	¥354,970	¥48,118	¥76,782	¥479,870
	Thousands of U.S. dollars			
	Gas Sales	LPG	Other	Total
For 2017:				
Net sales to external customers	\$2,398,964	\$412,197	\$674,857	\$3,486,018

(2) Information about geographic areas:

•Operating revenues

Not applicable

•Property, plant and equipment

The Company has omitted the disclosure of property, plant and equipment because property, plant and equipment in Japan account for more than 90% of the amount of property, plant and equipment reported in the consolidated balance sheets.

(3) Information about major customers:

Not applicable

Information about impairment losses on fixed assets in reportable segments

Not applicable

Information about goodwill in reportable segments

Not applicable

12 Certain lease transactions

As lessor:

Some of the consolidated subsidiaries have entered into finance lease contracts as lessor. A summary of the contracts under finance leases on a pro forma basis were as follows:

1. Finance lease

(1) Lease investment assets (current assets)

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Lease receivables	¥6,340	¥5,995	\$56,607
Estimated residual value	760	560	6,786
Interest income	(1,182)	(1,141)	(10,554)
Lease investment assets	¥5,918	¥5,414	52,839

(2) Recovery plans amount of lease receivables related to lease receivables and investment assets after the end of current fiscal year (current assets)

	Millions of yen					
	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
For 2017:						
Lease receivables	¥430	¥396	¥378	¥362	¥320	¥1,582
Lease investment assets	1,510	1,239	964	744	525	1,358
	¥1,940	¥1,635	¥1,342	¥1,106	¥845	¥2,940
For 2016:						
Lease receivables	¥427	¥400	¥366	¥349	¥333	¥1,644
Lease investment assets	1,479	1,232	958	701	496	1,129
	¥1,906	¥1,632	¥1,324	¥1,050	¥829	¥2,773
	Thousands of U.S. dollars					
	Due within one year	Due after one year through two years	Due after two years through three years	Due after three years through four years	Due after four years through five years	Due after five years
For 2017:						
Lease receivables	\$3,839	\$3,536	\$3,375	\$3,232	\$2,857	\$14,125
Lease investment assets	13,482	11,063	8,607	6,643	4,687	12,125
	\$17,321	\$14,599	\$11,982	\$9,875	\$7,544	\$26,250

Finance lease transactions that do not transfer the ownership of the leased property, commenced before April 1, 2008, the beginning date of the application of the accounting standard for lease transactions, and were accounted for with accounting treatment similar to that used for operating leases are summarized as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Lease income	¥120	¥120	\$1,071
Future lease commitments to be received (inclusive of imputed interests):			
Due within one year	120	120	1,071
Due after one year	1,320	1,440	11,786
	¥1,440	¥1,560	\$12,857
	Millions of yen		Thousands of U.S. dollars
	Acquisition cost	Accumulated depreciation	Net value
For 2017:			
Other facilities	¥1,900	¥868	¥1,032
For 2016:			
Other facilities	¥1,900	¥796	¥1,104
	Thousands of U.S. dollars		Thousands of U.S. dollars
	Acquisition cost	Accumulated depreciation	Net value
For 2017:			
Other facilities	\$16,964	\$7,750	\$9,214
	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Lease depreciation	¥72	¥72	\$643

13 Contingent liabilities

The TOHO GAS Group was contingently liable for bank loans with respect to guarantees for joint and several liability upon the default of others and for bank loans with respect to guarantees for housing loans of employees. At March 31, 2017 and 2016, these contingent liabilities were as follows:

	Millions of yen		Thousands of U.S. dollars
	2017	2016	2017
Guarantees for housing loans of employees	¥232	¥299	\$2,071
Guarantees for bank loans of Ichthys LNG Pty Ltd.	7,541	7,594	67,330
Guarantees for bank loans of MEET Europe Natural Gas, Lda.	2,875	—	25,670
Domestic unsecured notes due 2018 at a rate of 3.175%	10,000	5,000	89,286
Domestic unsecured notes due 2022 at a rate of 2.06%	10,000	5,000	89,286

14 Derivative transactions

The TOHO GAS Group has adopted policies restricting the use of derivatives and requiring the reporting of such transactions to the responsible officials of the Company. All derivative transactions outstanding at March 31, 2017 and 2016 were accounted for by hedge accounting in accordance with the accounting standard for financial instruments. The effectiveness of a hedge is evaluated by confirming the relationship between the hedge contract and the transaction hedged by that contract.

Hedge contract	Object of hedged transaction
Commodity swap	Purchase price of raw materials
Exchange forward contract	Purchase price of raw materials
Interest rate swap	Corporate bonds and bank loans

Derivative transactions to which hedge accounting was applied that were outstanding as of March 31, 2017 and 2016 are summarized as follows:

		Notional principal or contract amounts		
		Total	Over 1 year	Fair value
Hedge contract		Millions of yen		
For 2017:				
Commodity swap contracts				
(fixed rate payment, floating rate receipt)	.....	¥ 13,814	¥ —	(¥ 2,703)
Exchange forward contracts	.....	24,596	—	2,087
Interest rate swap contracts				
(fixed rate payment, floating rate receipt)	.....	9,161	9,161	(*2)
For 2016:				
Commodity swap contracts				
(fixed rate payment, floating rate receipt)	.....	¥ 27,628	¥ 13,814	(¥ 11,050)
Exchange forward contracts	.....	53,757	24,596	5,085
Interest rate swap contracts				
(floating rate payment, fixed rate receipt)	.....	5,000	5,000	122
Interest rate swap contracts	.....		
(fixed rate payment, floating rate receipt)	.....	10,677	8,677	(*2)
		Thousands of U.S. dollars		
Commodity swap contracts	.....	\$123,339	\$—	(\$24,134)
Exchange forward contracts	.....	219,607	—	18,634
Interest rate swap contracts	.....	81,795	81,795	(*2)

Notes:*1. Fair value was based principally on prices provided by the corresponding financial institutions.

*2. Derivative transactions such as interest rate swap contracts are accounted for by special hedge accounting such that the derivatives are not separated from the hedged bank loans. Therefore, the fair value of such derivative instruments is reflected in the calculation of the related bank loan.

15 Fair value of investment and rental property

The Company and some of its subsidiaries own land and office buildings for rent in Aichi and other prefectures. For the years ended March 2017 and 2016, in connection with those rental properties, the Company recorded rent revenues of ¥1,340 million (\$11,964 thousand) and ¥1,246 million, respectively. Rent revenues were included in the net sales account and the non-operating income account in the accompanying consolidated statements of income. Major rent expenses were included in the selling, general and administrative expenses account.

Information about fair value of rental property as of and for the years ended March 31, 2017 and 2016 was as follows;

	Millions of yen			
	Carrying value at the beginning of year	Net changes during the year	Carrying value at the end of year	Fair value at the end of year*
March 31, 2017	¥9,771	¥554	¥10,325	¥28,031
March 31, 2016	¥8,584	¥1,187	¥9,771	¥26,961
	Thousands of U.S. dollars			
	Carrying value at the beginning of year	Net changes during the year	Carrying value at the end of year	Fair value at the end of year*
March 31, 2017	\$87,241	\$4,947	\$92,188	\$250,277

*Fair value was based principally on real estate appraisal standards.

16 Subsequent events

1. Appropriation of surplus

On June 27, 2017, at the annual general meeting of shareholders of the Company, the following appropriations of surplus were approved:

	Millions of yen	Thousands of U.S. dollars
Cash dividends ¥5.00 (\$0.04) per share	¥2,677	\$23,902

2. Share buy-back

On April 28, 2017, the Board of Directors of the Company resolved to repurchase its shares pursuant to Article 156 of the Corporation Law as applied pursuant to Article 165, paragraph 3 as follows.

- (1) Types of shares to be repurchased: Common stock
- (2) Number of shares to be repurchased: Up to 3.7 million shares (representing 0.7% of outstanding shares (excluding treasury shares))
- (3) Value of shares to be repurchased: Up to ¥3 billion (\$26,786 thousand)
- (4) Period of repurchase: From May 8, 2017 to July 31, 2017

Based on the resolution, the Company repurchased its shares as follows.

- (1) Period of repurchase: From May 9, 2017 to July 20, 2017 (Commitment basis)
- (2) Number of shares repurchased: 3,700 thousand shares
- (3) Total value of shares repurchased: ¥2,994 million (\$26,732 thousand)
- (4) Method of repurchase: Market purchase on Tokyo Stock Exchange

3. Change in the number of shares per trading unit and consolidation of shares

TOHO GAS, at its Board of Directors' meeting held on April 28, 2017, resolved to change the number of shares per trading unit and make a partial amendment of the Articles of Incorporation and to submit the matter of the consolidation of shares to the 146th annual shareholders meeting on June 27, 2017. The resolutions were approved at the 146th annual shareholders meeting.

(1) Reasons for change in the number of shares per trading unit and consolidation of shares

All Japanese stock exchanges are promoting trading units to 100 shares for common stock for all domestic listed companies based on the "Action Plan for Consolidating Trading Units."

As a company listed on the Tokyo Stock Exchange and the Nagoya Stock Exchange, the Company respects the objectives of the Plan and has taken steps to change its single trading unit from 1,000 shares to 100 shares and to consolidate its shares on the basis of 1 share for every 5 shares to adjust the trading unit to an appropriate price level.

(2) Particulars of change in the number of shares per trading unit

The number of shares per trading unit will be changed from 1,000 shares to 100 shares as of October 1, 2017.

(3) Particulars of consolidation of shares

(i) Type of shares to be consolidated

Common stock

(ii) Consolidation ratio

On October 1, 2017, the shares held by the shareholders of record as of September 30, 2017 will be consolidated at the ratio of 5 shares to 1 share.

(iii) Number of shares reduced through consolidation

Outstanding shares before consolidation (as of March 31, 2017)	538,196,429 shares
Number of shares reduced through consolidation	430,557,144 shares
Outstanding shares after consolidation	107,639,285 shares

(Note 1) "Number of shares reduced through consolidation" and "Outstanding shares after consolidation" are theoretical values calculated based on "Outstanding shares before consolidation" and the consolidation ratio.

(Note 2) The Company announces that its Board of Directors' meeting held on March 30, 2017 approved the retirement of treasury stock of 2,730,000 shares on April 28, 2017, and the number of outstanding shares after the retirement will be 535,466,429 shares. Considering the retirement of treasury stock, "Outstanding shares after consolidation" will be 107,093,285 shares.

(iv) Treatment of fractional shares

If any fractional shares arise as a result of the consolidation of share, The Company will sell all such fractional shares and distribute the proceeds to shareholders having fractional shares in proportion to their respective fractions.

(4) Schedule for change in the number of shares per trading unit and consolidation of shares

The Board of Directors' meeting	April 28, 2017
The 146th annual shareholders meeting	June 27, 2017
Effective date of change in the number of shares per trading unit and consolidation of shares	October 1, 2017

(5) Impact on per share information

Per share information based on the assumption that this consolidation had been implemented at the beginning of the previous fiscal year is presented as follows for the previous period and the current period.

	FY2015 (Apr. 2015 -Mar. 2016)	FY2016 (Apr. 2016 -Mar. 2017)	FY2016 (Apr. 2016 -Mar. 2017)
Net income per share	¥397.06	¥164.87	\$1.47

(Notes) Diluted net income per share is not disclosed as the Company has no dilutive common shares.

Independent Auditor's Report

TOHO GAS CO., LTD. and Consolidated Subsidiaries

To the Board of Directors of TOHO GAS Co., Ltd.:

We have audited the accompanying consolidated financial statements of TOHO GAS Co., Ltd. and its consolidated subsidiaries, which comprise the consolidated balance sheets as at March 31, 2017 and 2016, and the consolidated statements of income, statements of comprehensive income, statements of changes in net assets and statements of cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in Japan, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in Japan. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, while the objective of the financial statement audit is not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of TOHO GAS Co., Ltd. and its consolidated subsidiaries as at March 31, 2017 and 2016, and their financial performance and cash flows for the years then ended in accordance with accounting principles generally accepted in Japan.

Convenience Translation

The U.S. dollar amounts in the accompanying consolidated financial statements with respect to the year ended March 31, 2017 are presented solely for convenience. Our audit also included the translation of yen amounts into U.S. dollar amounts and, in our opinion, such translation has been made on the basis described in Note 1 of the Notes to the Consolidated Financial Statements.

KPMG AZSA LLC

KPMG AZSA LLC

July 28, 2017

Nagoya, Japan