

### **(13) Risks Associated with Information Systems and Information Security**

In ITOCHU, a code of conduct concerning the handling of information is set for all directors and employees and high priority is placed on maintaining a high information security level in the Company. ITOCHU has established an information system to facilitate the sharing of information internally within ITOCHU and externally with clients, and to improve the efficiency of operations. In order to maintain a secure operation of ITOCHU's information systems, ITOCHU has established a firewall to prevent outside intrusions to the network, established security guidelines, and have developed crisis control measures. Despite these measures, ITOCHU cannot completely avoid the possibility of unauthorized access from the outside, the leakage of sensitive company information due to computer viruses, or operational failure of the system due to damage to information system equipment arising from natural disasters or accidents or from trouble with telecommunica-

tions circuitry. If such events occur, this could cause a deterioration of operational efficiency and depending on the seriousness of the damage, have a serious adverse effect on the financial position and results of operations of ITOCHU.

Moreover, ITOCHU gathers and maintains personal information in the course of ITOCHU's operations. Such information relates to the Company, retailing, credit and financing, and services offered. In conjunction with the enactment of laws pertaining to the safeguarding of personal information on April 1, 2005 (Personal Information Protection Act), ITOCHU is making even greater efforts to safeguard personal information. However, ITOCHU cannot completely avoid the possibility of personal information being transmitted outside the Company due to improper acts by employees or intrusion from the outside, and the consequent fraudulent use or diversion of such information. If such events occur, ITOCHU would face a grave loss of public trust, and could face serious adverse effects to the financial position and results of operations.

### **Critical Accounting Policies**

The Company's consolidated financial statements are prepared in conformity with U.S. GAAP. In preparation of the consolidated financial statements, the management of the Company is required to make a number of estimates, judgments and assumptions that affect the reported amounts of assets, liabilities, contingent assets and liabilities as of each balance sheet date, and revenues and expenses in each reporting period. Management periodically verifies and makes a review of its estimates, judgments and assumptions based on the available information that is considered to be reasonable by judging from historical experiences and circumstances. These estimates, judgments and assumptions, however, which are often accompanied by uncertainties, may differ from actual results. These differences may have an effect on the Company's consolidated financial statements and performances of every operating segment. The following accounting policies related to estimates, judgments and assumptions that management believes may materially affect consolidated financial statements.

#### ***Evaluation of Investments***

Investment balance and profit from investments are important factors in the Company's consolidated financial statements and therefore, accounting judgment on evaluation of investments has a substantial impact on the Company's consolidated financial statements. ITOCHU evaluates marketable securities based on their fair values. The difference between carrying amount and fair value is reported in the consolidated statements of operations for trading securities, while differences net of tax are reported in stockholders' equity as unrealized holding gains on securities, for available-for-sale securities. When ITOCHU judges that the price decrease of marketable securities is other than temporary, considering severity and duration of decline in the fair value against carrying amount, impairment losses are recognized for the devaluation of this value.

For the impairment of non-marketable securities, judgment of an other-than-temporary decline is conducted after a comprehensive consideration of the magnitude of the decrease in terms of net asset value, the financial conditions of the invested companies, and the outlook for their future performance.

For the impairment of marketable investments in equity-

method investments, in accordance with U.S. Accounting Principles Board Opinions No.18, as is the case for impairment of long-lived assets, ITOCHU judges whether or not a price decrease is other than temporary not only by measuring the magnitude of the decrease in market value but also comprehensively considering the possibility of collection based on the estimated future cash flows generated from the investment.

The management of the Company believes these investment evaluations are rational. However, difference in estimates such as estimated future cash flows due to unforeseen changes in business conditions may impair the value of investments and have a material impact on the Company's consolidated financial statements.

#### ***Provision for Doubtful Receivables***

Trade receivables including notes and accounts, in addition to loans, represent a large amount in the Company's consolidated balance sheets, and provision for doubtful receivables is an important factor in the Company's consolidated statements of income. Therefore, accounting judgment on evaluation of receivables has a substantial impact on the Company's consolidated financial statements.

In the Company, the credit department of each Division Company, which is independent of business departments of each Division Company, manages and evaluates credit risk from both quantitative and qualitative perspectives, monitoring regularly the credit limit and the status quo of trade receivables, and reviewing regularly the status quo of debt collection and delinquency to discuss and record the required provision for doubtful receivables. The Company estimates the recoverable amount and records the required provision for doubtful receivables, after comprehensively considering the status of collection, past insolvency record, financial conditions of debtors and value of collateral.

The management of the Company believes that these estimations of provisions for doubtful receivables are rational. However, deterioration of the debtors' financial conditions and decreases in estimated collateral value due to unpredictable changes in business conditions may reduce the recoverable amounts from the latest estimation, and an increase in provision for doubtful receivables may have a material impact on the Company's consolidated financial statements.