



# Dedicated to sustainability

Sustainability Report 2004



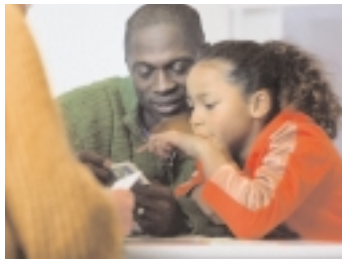
**PHILIPS**

# Our way of doing



## **Social responsibility**

We seek innovation for our customers and consumers, create an environment that helps our employees reach their full potential and are active in the communities where we live and work. And we explore business opportunities with sustainability as a driver to benefit people in advanced, emerging and developing markets.



## **Environmental responsibility**

We regard environmental improvement as an opportunity for innovation, and we work to minimize the impacts of products, processes and services. With a tradition of sound environmental policy for more than 30 years, we are guided by the basic principle that prevention is better than cure.

# business



## **Economic responsibility**

We are working to transform Philips into a truly market-driven healthcare, lifestyle and technology company. Our priority is to create sustainable value for our stakeholders. Going forward, our focus on innovation is providing us with a basis for stronger growth across all our product divisions.

We firmly believe that socially and environmentally responsible behavior contributes to sustained profitable growth and value creation. That's why we are embedding sustainability thinking and acting throughout the organization.

Sustainability is built into our heritage, our values and our commitment to improve the quality of people's lives. We have long been integrating economic prosperity, environmental quality and social equity – balancing these sometimes-competing demands.

## About this report

Sustainability is defined as “meeting the needs of the present generation without compromising the ability of future generations to meet their own needs.” Sustainable development – which is considered the path to sustainability – is the simultaneous pursuit of economic prosperity, environmental quality and social equity. Companies that pursue this path are known as sustainable entrepreneurs. Focusing on sustainability often requires dealing with the sometimes-competing demands of integrating social, environmental and economic responsibility, and balancing short- and long-term interests.

Royal Philips Electronics started external reporting on its environmental performance on a yearly basis covering the year 1998. Since 2002, the company provides information annually on its sustainability activities in a comprehensive report comprised of social, environmental and economic sections. This report provides information on the company's sustainability activities for the 2004 fiscal year, running from January 1, 2004 to December 31, 2004.

Philips views this report as a valuable tool for maintaining a dialogue with a variety of interested parties, including shareholders, customers, business partners, governmental and non-governmental organizations and, of course, Philips employees around the world, who work daily to improve the company's performance.

In compiling this report for 2004, Philips has followed relevant best practice standards and international guidelines, including the Global Reporting Initiative's (GRI) 2002 Sustainability Reporting Guidelines. Philips also has taken valuable comments from inside and outside the company into account. Specific attention has been paid in crafting this report to show how sustainable development is an integral part of the company's strategic direction and how we embed it throughout our organization. In addition, we have made considerable strides in reporting on our social performance and in providing information about our stakeholder dialogue activities.

This Sustainability Report 2004 is externally verified by KPMG, in line with previous reports. Their non-financial

assurance engagement, which was conducted in accordance with the International Standard on Assurance Engagements ISAE 3000, covers all of the information in the report, both quantitative and qualitative. KPMG's Assurance Report, which describes the work undertaken and their conclusions, can be found on page 85. We will continue to improve the quality of our sustainability reporting. We anticipate that we will have the report independently reviewed in the future as well.

Readers are invited to support our improvement process with their feedback. Please contact the Corporate Sustainability Office via our website [www.philips.com/sustainability](http://www.philips.com/sustainability) or by e-mail at [philips.sustainability@philips.com](mailto:philips.sustainability@philips.com)

## Scope of this report

This report describes the performance of the Philips Group with regard to sustainability. It covers the total of the consolidated Philips activities, following the consolidation criteria as described on page 97 of the Philips Annual Report 2004. Unconsolidated companies, including 50/50 joint ventures, are not reported. Environmental results are limited to production activities for those manufacturing sites with more than 50 industrial employees.

The Philips Group consists of the following product sectors for the reporting year 2004:

- Medical Systems
- Domestic Appliances and Personal Care
- Consumer Electronics
- Lighting
- Semiconductors
- Other Activities

This report includes selected information on the financial performance of the Philips Group. For full understanding of the financial performance, please refer to the Philips Annual Report 2004.

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## Forward-looking statements

This report contains certain forward-looking statements with respect to the financial condition, results of operations and business of Philips and certain of the plans and objectives of Philips with respect to these items. By their nature, forward-looking statements involve risk and uncertainty because they relate to events and depend on circumstances that will occur in the future. There are a number of factors that could cause actual results and developments to differ materially from those expressed or implied by these forward-looking statements.

Statements regarding market share, including as to Philips' competitive position, contained in this document are based on outside sources such as specialized research institutes, industry and dealer panels, etc. in combination with management estimates. Rankings are based on sales unless otherwise stated.

## Interviews

Philips does not necessarily agree with the opinion of the writers of bylined articles or those interviewed for sidebar articles in this report.





“We see sustainability  
as part of our way  
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**Dear Stakeholder,**

2004 was a year of major progress for Philips, not only in terms of our financial results, but also with respect to the progress we are making in embedding sustainability throughout the company.

It is rewarding to see our efforts recognized by external organizations. We are proud to have been selected – for the second consecutive year – as the top company in our market sector in the Dow Jones Sustainability Index. This achievement is particularly significant for us because we know that many companies have been making substantial efforts in this area. Ranking number one is evidence of a solid team effort by a great number of employees throughout our product divisions, regions and corporate functions.

We have been hard at work to drive sustainability thinking and acting at all levels of the organization. At the same time we continue to build knowledge and explore sustainability as a driver for business development. To do this, we are using an embedded model approach to fully integrate sustainability in all of our day-to-day business activities.

### **Fulfilling our commitments**

We see sustainability as part of our way of doing business. While we know we have a long way to go, we are pleased with the progress we are making. It's about continuously striving to fulfill our commitments, and I am pleased to share with you an overview of our results.

### **Listening to our stakeholders**

Because sustainability requires open, honest dialogue with our internal and external stakeholders, we are working to create more structure around stakeholder interactions. This is critical in helping us effectively manage the issues that are important to our various constituencies.

In last year's report I committed to developing action plans based on the results of our reputation survey. After analyzing the data, we formed a Reputation Committee, which I chair. My colleagues and I have decided to focus on the main driver for reputation – performance management. We have made good progress there in 2004.

For all key countries surveyed, we have established specific action plans, which include stepping up our dialogue with stakeholders through consistent communication about mission, vision and strategy, and our progress with its implementation, while having an open mind for the feedback we receive.

Furthermore, the results of the reputation research are being used as input for change throughout the company. For example, the survey data has been valuable in supporting our decisions around our new brand positioning and brand promise, 'Sense and simplicity.'

### **Sense and simplicity**

This simple phrase reflects our understanding that people want technology that gets the job done without drawing attention to itself. Products that are relevant and meaningful to them – that make sense in the context of their lives. Solutions that make it easy to enjoy the enhanced experiences that technology can offer.

Customers in the healthcare, lifestyle and technology markets that we operate in want common sense from us. That's why we are promising to make technology easier to experience and designed around people, while still remaining advanced. This is in keeping with our mission to improve the quality of people's lives.

“We are committed to improving the quality of people’s lives with sustainability as a cornerstone of our strategy.”

#### **Fostering partnerships**

We are continuing to foster partnerships with a broad range of stakeholders – working closely with customers, expanding alliances and partnerships to enter new markets, linking with content and service providers, developing partnerships for manufacturing and technology, and collaborating with leading institutes and universities. In the coming pages you will hear from some of our partners on our joint efforts.

#### **Supplier management**

We see suppliers as forming part of our sustainability strategy. After all, we can only stick to our principles on sustainability if they do too.

We developed a comprehensive supplier sustainability involvement program in 2003, taking the first step in its implementation – creating awareness of our sustainability policies, goals and efforts. One of the key targets for 2004 was to take the next step – suppliers committing to our Philips Supplier Declaration on Sustainability, which outlines the essential principles in the areas of health and safety, the environment and working conditions, including child labor. We are very encouraged that all of the initial group of key suppliers to whom we distributed the document have agreed to adhere to its principles. We have moved into the third and fourth steps – the rollout of a self-assessment tool, which enables suppliers to evaluate their sustainability performance, and the use of external audits.

#### **General Business Principles**

During 2004 we completed the worldwide rollout of the new version of our General Business Principles. These have been translated into the local language – and are an integral part of the labor contract – in virtually all countries.

We have established standardized complaint reporting and escalation procedures. With this in place, we are now able to include information on reported violations in this report.

#### **Health and safety**

We have made significant progress in implementing our program for standardized data collection and reporting of health and safety data throughout the company. We are pleased to provide first results for two important parameters: lost work time rate and lost workday injuries.

#### **Diversity and inclusion**

Reflecting comparatively recent shifts in society and the global economy, diversity and inclusion has been steadily gaining importance within Philips. We have appointed a Vice President of Global Diversity and Inclusion, and I chair our Diversity and Inclusion Council.

While the number of women in top management has remained at 5%, the number of leadership top potential female employees is more than 10%. This will help us achieve our target of raising the number of women in senior management to at least 10% by 2008.

We firmly believe that by incorporating diversity and inclusion into our overall leadership approach, we will achieve our goals.

#### **Social investments**

In 2004 we funded more than 200 social investment projects from 47 countries in all four regions. About 75% of the projects fell within our two areas of focus – providing access to healthcare and education, particularly for the underprivileged. You will find a representative selection of our projects in this report.



Employees at a town hall meeting in Shanghai welcome Gerard Kleisterlee.



## EcoVision

We are continuing our progress in the environmental area, working to meet the targets set forth in our EcoVision 2002-2005 action program. We are pleased with our results overall, including launching 21 Green Flagship products in 2004, compared with eight in 2003.

On the manufacturing side, we also have made progress in reducing our environmental impact. For example, we have reduced Category I substances – those that we have restricted in production worldwide because they are considered harmful to the environment – by 62% compared with 2003.

While working to achieve our current EcoVision goals, we have started the process of setting the agenda for our next four-year program, EcoVision 2006-2009.

## Financial performance

Driven by our focus on operational performance and cost management, our financial results showed considerable improvement in 2004, delivering a return well in excess of our cost of capital. Going forward, our focus on innovation is providing Philips with a basis for stronger growth across all our divisions.

## Exploring new business opportunities

In last year's report I said that I was personally challenging Philips employees to explore new business opportunities and new markets with sustainability as a key driver. We asked employees to develop a business case for projects that will benefit people and contribute to our growth.

Our progress during 2004 can be summed up in two words: learning and discovery. We made considerable progress with two pilot projects, one in India and another in Brazil. We have laid a strong foundation, strengthening partnerships and reviewing business models. In 2005 we will work to speed up this process and drive it through the organization, engaging cross-functional teams from R&D, the regions and product divisions.

## Our way forward

For 2005 we have established a solid management agenda for sustainability and identified our first set of Key Performance Indicators at company level to track our performance on the agenda's major issues. This will support us in making further progress on our commitment to improve the quality of people's lives with sustainability as a cornerstone of our strategy. We've been doing just that for more than a century and are dedicated to carrying on this tradition.

Gerard Kleisterlee,  
*President*

# About Philips

In 1891, we lit up the world. Since then, technology has been advancing, simplifying your life in ways never imagined. At Philips, we are committed to delivering products and solutions that are easy to experience, designed around you and advanced. We believe simplicity can be a goal of technology. It's certainly our goal at Philips. It just makes sense.

## Our heritage

Sustainability also makes sense at Philips. Our company's founders, Anton and Gerard Philips, saw no difference between business and sustainable business. Putting people at the center was inherent to their way of working. You could say sustainability is in our DNA. It's built into our heritage, our values and our commitment to improve the quality of people's lives.

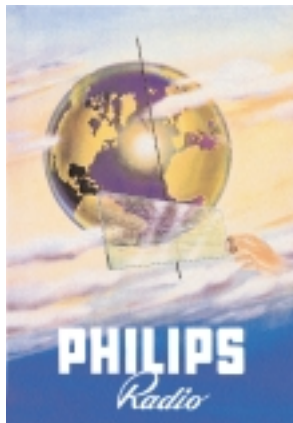
We have long been integrating economic prosperity, environmental quality and social equity – balancing these sometimes-competing demands with a clear view on sustainable value creation.

In recent years, we have been hard at work to create One Philips – a single, focused and clearly identifiable company geared to delivering sustained profitability in the key areas of healthcare, lifestyle and technology. But our leadership in these areas is hardly new.

## Aiding public health

Back in 1917 the company's Physics Laboratory began helping Dutch radiologists by repairing faulty X-ray tubes. Between 1922 and 1924 Philips developed a new, superior X-ray tube. The cylindrical "metalix" tube, as it was called, afforded better protection against scattered radiation and the dangers associated with the use of high voltages. In 1928, the Radiological Society of North America awarded the head of the Philips X-ray research group, Albert Bouwers, its annual gold medal for special services.

Anton Philips strongly backed the X-ray division. He accepted losses year after year, seeing the X-ray industry as a fruitful area for the company, "which we must persevere with and even splash out some money on." Anton attached great importance to X-ray diagnostics as an aid to public health, particularly in the fight against the spread of tuberculosis. Thanks to a program to X-ray all the Philips workers in Eindhoven, the city's tuberculosis cases fell far below average.



### Changing lifestyles

With outside antennas and tubes, the complicated, bulky radios of the 1920s looked like scientific instruments. Philips changed all that when we started to produce radios in 1927. The first set we brought on the market was a completely new concept. There were no outside parts. The tubes and antenna coils were inside a small rectangular case that could easily be placed on a small table or even hung on the wall like a painting. The radio's innovative design meant the listener had only a few knobs to switch the set on, select a station and adjust the volume of the beautifully designed external loudspeaker. The number of radio tubes could be kept small thanks to the company's newly developed amplification tube, the famous Pentode. By 1933, Philips was the largest producer of radios and radio lamps in the world.

### Meaningful technology

The company's technological prowess was evident when it was founded in 1891 to meet the growing demand for light bulbs, created by the commercialization of electricity. The goal was to produce cost-effective, reliable light bulbs for everyone.

Since then, Philips' substantial investment in R&D has generated many breakthrough innovations, including the Compact Cassette system and the laser based optical disc systems CD-Audio, CD-ROM, CD-R/RW, SACD and various DVD formats.

### Our organization

The activities of the Philips group are organized in six operating product divisions: Medical Systems, Domestic Appliances and Personal Care, Consumer Electronics, Lighting, Semiconductors and Other Activities. Each is responsible for the management of its business worldwide.

The sector Other Activities comprises various activities and businesses not belonging to another product sector. It consists of four main groups of activities: the Technology Cluster (such as Philips Research, Intellectual Property & Standards and Philips Centre for Industrial Technology), Corporate Investments (such as Assembléon and Philips Enabling Technologies Group), Global Service Units and Miscellaneous (such as Optical Storage). It also comprises various (remaining) activities from businesses that have been sold, discontinued, phased out or deconsolidated in earlier years.

## Highlights

- Sales: EUR 30,319 million
- Multinational workforce: 161,586 employees
- Market capitalization: EUR 25 billion
- Net operating capital: EUR 7,192 million
- Stockholders' equity: EUR 14,860 million
- Net debt: Group equity ratio of 1:99
- Net income: EUR 2,836 million, or EUR 2.22 per common share
- Research and development expenditures: 8.4% of sales, or EUR 2,534 million
- New patents filed in 2004: 3,065
- Worldwide patent portfolio (individual patents) end 2004: 115,000
- Licenses income (from patents): EUR 478 million

Philips products are sold in about 150 countries, to a large extent through owned national sales and service organizations. A minor part is sold by independent local distributors. Industrial activities are spread widely across regions, comprising 141 manufacturing sites in 32 countries as of year-end 2004. Philips product divisions have at their disposal development laboratories and implementation departments in more than 20 countries throughout the world. These centers fuel our technology base.

Region and country organizations support the Philips businesses.

## Participations

Philips is involved in the following key joint ventures and participations:

LG.Philips LCD	44.6%
LG.Philips Displays	50%
Atos Origin	15.4%
Lumileds Lighting	48%
TSMC (Taiwan Semiconductor Manufacturing Co. Ltd.)	19%
NAVTEQ	34.8%
FEI Company	26%
InterTrust Technologies Corporation	49.5%
Philips Medical Capital	40%

At year-end 2004, the Corporate Venturing portfolio comprised some 10 companies in which we have a minority stake and, in some case, an active business relationship.

These joint ventures and participations are not included in the scope of this report.

## Industry leadership

Philips has leading market positions in many areas. Our sales are predominantly under the Philips brand. Products from our Domestic Appliances and Personal Care division are sold globally under the Philips brand and other brands (such as Sonicare worldwide and Norelco in the United States). A minority of our sales in consumer electronics is non-Philips branded, while sales to OEM (Original Equipment Manufacturer) customers are significant for monitors and other IT-related peripherals.

In December 2004, Philips and TPV Technology Limited have signed a Letter of Intent for the PC monitor and entry level Flat TV segments. Per the agreement, TPV will take over the responsibility of Philips' existing OEM monitor business.

## Our market positions

(value based, 2003)	World	Europe
Lighting	1	1
Consumer Electronics (audio/video)	3	1
Monitors (branded and OEM)	5	3
DVD Recorders	1	1
Steam irons	2	2
Dental care (electric toothbrushes)	2	2
Semiconductors	10	6
Medical imaging equipment	2	1

## Our legal and shareholder structure

Royal Philips Electronics common stock (1,316,070 thousand shares in total) is listed on the Euronext Amsterdam and the New York Stock Exchange.

The common shares are held by shareholders worldwide in bearer and registered form. Outside the United States, shares are held primarily in bearer form. As of the end of 2004, approximately 89% of the total number of common shares was held in bearer form. This means that we do not have information on the profile of our shareholders. No person or group is known to the company to be the owner of more than 5% of the common shares.

As of the end of 2004, there were 10 authorized and issued priority shares, held by the Dr. A. F. Philips Foundation, and 3,249,975 thousand preference shares authorized, of which none were issued. A proposal shall be made to the Annual General Meeting of Shareholders to be held on March 31, 2005 to amend the current articles of association of Philips. Upon the shareholders meeting approving this amendment, the priority shares will be cancelled pursuant to the Amended Articles of Association. For a full description of the rights of the owners of these priority and preference shares, please see the Annual Report 2004.

## Corporate governance

For many years now Philips has pursued a consistent policy to enhance and improve its corporate governance – including its disclosure practices – in line with best practices. In its two-tier corporate structure, executive management is entrusted to the Board of Management under the supervision of the independent Supervisory Board. Both boards are accountable to the General Meeting of Shareholders for the performance of their functions. All outstanding shares carry voting rights. Continuously striving to improve relations with its shareholders, the company aims for a fair disclosure policy and follows an active investor relations approach.

Comprehensive internal procedures, compliance with which is supervised by the Supervisory Board and its Audit Committee, are in place for the preparation and publication of financial results and ad-hoc financial information. The annual financial statements, observing Dutch law and applying US GAAP, are presented for discussion and adoption to the shareholders meeting. A separate Annual Report on Form 20-F, certified by both the Chief Executive Officer and the Chief Financial Officer, is filed with the US Securities and Exchange Commission.

The company, which is required to comply with the US Sarbanes-Oxley Act and related regulations, has disclosed and maintains a policy of strict separation between the auditing and non-auditing functions of its external auditor. The external auditor, which is assessed by the Supervisory Board and its Audit Committee, is appointed by the General Meeting of Shareholders as required by Dutch law. A proposal shall be made to the March 2005 Annual General Meeting of Shareholders to re-appoint KPMG Accountants N.V. for an additional three years.

Against the background of the continuous endeavors to improve the company's corporate governance, and in connection with the implementation of the Dutch Corporate Governance Code of December 9, 2003 and new Dutch legislation, a proposal will be made to the March 2005 Annual General Meeting of Shareholders to amend the current articles of association of the company.

The company addresses its overall corporate governance structure and the way it implements the Dutch Corporate Governance Code on pages 195 to 208 of the Annual Report 2004.

#### Shareholder meetings

A General Meeting of Shareholders is held at least once a year to discuss the Annual Report – including the report of the Board of Management, the annual financial statements with explanation and appendices, and the report of the Supervisory Board – any proposal concerning dividends or other distributions, the appointment of members of the Board of Management and Supervisory Board (if any), important management decisions as required by Dutch law, and any other matters proposed by the Supervisory Board, the Board of Management, the Meeting of Priority Shareholders (until the Amended Articles of Association enter into force) or shareholders in accordance with the provisions of the company's articles of association.

The agenda of the General Meeting of Shareholders shall contain such business as may be placed thereon by the Board of Management, the Supervisory Board or the Meeting of Priority Shareholders, and agenda items will be explained where necessary in writing. In accordance with the articles of association and Dutch law, requests from shareholders for items to be included on the agenda will generally be honored, subject to the company's rights to refuse to include the requested agenda item under Dutch law, provided that such requests are made at least 60 days before a General Meeting of Shareholders to the Board of Management and the Supervisory Board in writing by

shareholders representing at least 1% of the company's outstanding capital or, according to the official price list of Euronext Amsterdam N.V., representing a value of at least EUR 50 million.

The General Meeting of Shareholders is held in Eindhoven, Amsterdam, Rotterdam or The Hague no later than six months after the end of the financial year.

Extraordinary General Meetings of Shareholders may be convened by the Supervisory Board or the Board of Management if deemed necessary and must be held if the Meeting of Priority Shareholders (until the Amended Articles of Association enter into force) or shareholders jointly representing at least 10% of the outstanding share capital make a written request to that effect to the Supervisory Board and the Board of Management, specifying in detail the business to be dealt with.

The Board of Management and the Supervisory Board are required to provide the General Meeting of Shareholders with all requested information, unless this would be prejudicial to an overriding interest of the company. If the Board of Management and the Supervisory Board invoke an overriding interest, reasons must be given.

#### Shareholders' Communications Channel

Philips was one of the key companies in the establishment of the Shareholders' Communication Channel – a project of Euronext Amsterdam, banks in the Netherlands and several major Dutch companies to simplify contacts between a participating company and its shareholders.

Philips will use the Shareholders' Communication Channel to distribute the Agenda for this year's General Meeting of Shareholders as well as an instruction form to enable proxy voting at said Meeting.

#### Strengthening our sustainability governance

We have been continuing to strengthen our sustainability governance. Full details are provided in the section titled 'Sustainability at Philips,' beginning on page 16.

#### Business Excellence

The Philips way to achieve Business Excellence aims to deliver sustainable performance improvement at world-class levels for all stakeholders. Driving for continuous process improvement has become our way of working.

The European Foundation for Quality Management (EFQM) and Philips announced a partnership to share

# Resolving Competing Stakeholder Concerns through an Integrated Strategic Performance and Enterprise Risk Management System

By Dr. Carolyn Kay Brancato

Dr. Brancato is Director, Global Corporate Governance Research Center, The Conference Board. The Conference Board's Enterprise Risk Management study will be released during the first quarter of 2005.



Companies inundated by Sarbanes-Oxley requirements and compliance issues, are beginning to take a step back and assess not only their traditional performance measurement systems, but also their strategy and enterprise risk management systems. Integrating these systems is critical and can provide an added benefit – a tool for companies to balance the competing demands of their various stakeholders.

Establishing a systematic strategic performance measurement system is the first step. This involves creating a 'dashboard' of the measures that define the company's ability to create value, including both financial (earnings growth, return on investment, etc) and non-financial measures (quality improvements, intellectual capital, customer satisfaction, etc.).

Boards will have a smaller number of measures, while managers will 'drill down' into those measures under their control. Certain new metrics (and the methods to collect them) may have to be created, but many companies are already collecting much of the data they require to decide upon and track strategic performance measurements.

The second step is to develop an Enterprise Risk Management (ERM) system that can be laid on top of these strategic performance measures. Companies are faced with a number of legal requirements shaping the development of such systems. First, are the evolving duties of care, loyalty and good faith under corporate law. US courts have begun to look more

carefully at issues of good faith, requiring directors to search out and implement best practices. The combined effect is to force directors and executives to become more proactive in their oversight responsibilities.

In addition, the Sarbanes-Oxley Act was enacted in response to Congressional perception that corporations had a lack of control over the quality and accuracy of disclosure. Sarbanes-Oxley was intended to address failures to prevent fraud and abuses of the system – in essence, a failure to identify material risks and establish systems or procedures to mitigate these risks or prevent them from occurring. The final Sarbanes-Oxley Act framework, however, focuses on internal controls, rather than on the broader focus on strategic risks in an overall enterprise risk framework. Similarly, the revised New York Stock Exchange corporate governance listing standards require an internal audit function, as well as the delivery to management and the audit committee of assessments of the company's risk and management processes and systems of internal control.

## Enterprise Risk Management System

The Conference Board is completing a major survey of 276 risk officers at companies in the US, Europe and Canada. Of these, only 22% have a fully developed and robust ERM program. The degree of ERM integration with corporate practices is found to be the biggest challenge. Only 16% of companies surveyed have integrated ERM with their strategic planning, only 4% with their stakeholder

communications, their management scorecards and remuneration.

Steps required to build an effective ERM system involve, first, establishing a risk 'inventory.' An organization's tolerance for risk will vary with its strategy, evolving conditions in its industry and markets and its organizational culture and external factors. Management's responsibility is to determine which risks, and how much of each of them, the organization should take, and then to re-evaluate those choices as circumstances change. Information should be provided to the board that arrays the risks against the probabilities of occurrence and associated losses. Equipped with a set of success measures and an inventory of risks, companies can establish a 'heat map' that correlates risks with earnings exposure.

Finally, combining both processes of identifying strategic performance measures and subjecting them to an ERM risk analysis can be used to weight and evaluate claims of competing constituencies. For example, as environmental risks continue to be more formally analyzed and potential risks identified and quantified, boards and managements can use this information to balance competing demands made by other corporate constituencies. This leads to more thoughtful, comprehensive and transparent decision making, which in itself may reduce the risks of dealing with these constituencies and improve the perception of the corporation's fairness and transparency.



Philips best-in-class business excellence Process Survey Tools (PSTs). This move will make the Philips PSTs available through the EFQM to a wider business audience. The EFQM sees the Philips business process tools as setting a standard in quality management, and the partnership demonstrates that Philips quality not only shows in its products, but also in its business processes.

As one of the founding members of EFQM, Philips has applied quality management approaches for many years. The launch of our BEST (Business Excellence through Speed and Teamwork) program in 1999 brought our improvement methodologies under one umbrella and provided the organization with a common way of working to continuously enhance business performance.

#### General Business Principles Review Committee

The Philips General Business Principles govern the company's business decisions and actions throughout the world, applying equally to corporate actions as well as the behavior of individual employees when on company business.

The Board of Management has assigned final responsibility for coordination of all General Business Principles-related issues to the General Business Principles Review Committee, chaired by the Secretary to the Board of Management/Chief Legal Officer, who is a member of the Group Management Committee and the Sustainability Board.

#### Philips General Business Principles

The Philips General Business Principles (GBP) incorporate the fundamental principles on which all Philips activity is or should be based.

Responsibility for compliance with the Principles rests first and foremost with the management of each business. Every country organization and major production site has appointed a Compliance Officer. Confirmation of compliance with the GBP is an integral part of the annual Statement on Business Controls that has to be issued by the management of each organizational unit.

During 2003 we reviewed and updated our General Business Principles, including all relevant procedures. Prior to publication, the new edition of the Philips General Business Principles was submitted to Amnesty International and EIBE (European Institute for Business Ethics of Nyenrode University) for their expert comments. Reactions were positive, particularly regarding the incorporation of a human rights clause (International Labour Organization

Core Conventions) and the overall balance and consistency of the approach taken.

The Board of Management adopted the new edition of the General Business Principles in December 2003, and in February 2004 – following approval by the Supervisory Board – the President wrote to product division and country management to begin the launch process.

#### Updated Principles rolled out

Throughout 2004, significant progress was made in implementing and embedding the new GBPs issued at the end of 2003 within the global Philips organization. The GBPs were translated into the local language in all but two countries, and these two – Malaysia and Greece – have scheduled translation for the first quarter of 2005. In all but four countries (Austria, Belgium, France and Switzerland), the GBPs were distributed to all employees; however in these countries distribution will be complete in early 2005.

The new GBPs are now considered an integral and formal part of the employment contract for employees in all countries except four. Three of these four countries (Chile, Colombia and Mexico) are unable to enforce this due to local legislation. In the remaining country, Belgium, the GBPs are considered part of the contract for many but not all employees, but many of the principles are reflected in Belgian criminal and labor law. All countries consider dismissal a possible sanction in the event of a serious violation.

To help increase worldwide awareness of the General Business Principles, the Review Committee has developed a template for a poster, which can be produced locally, to promote the General Business Principles and highlight the role of the Compliance Officer. Consistent use of this poster throughout the world will provide maximize impact.



To drive the practical deployment of the Principles, we have published detailed guidelines in what we call our GBP Directives, which include the Purchasing Code of Ethics and the Financial Code of Ethics. To encourage compliance with the our standards of transparency and accountability by all employees performing important financial functions, the Financial Code of Ethics contains, among other things, standards to promote honest and ethical conduct and full, accurate and timely disclosure procedures to avoid conflicts of interest.

We developed a new dilemma-training casebook in 2004 to heighten awareness and understanding of the general issue of business ethics and, more specifically, to promote compliance with the Philips GBP. This casebook is also widely used in introductory courses for new employees. Within our Medical Systems division, e-learning tools are deployed to ensure that the new GBP are embedded throughout the organization, and other parts of Philips are expected to adopt this methodology in the coming year.

#### Complaint reporting and escalation procedures

Further, during 2004 we took a number of fundamental steps to encourage full compliance. To eliminate confusion and inconsistency regarding what has to be reported, a worldwide database for the standardization of the worldwide GBP data collection and reporting has been developed under the responsibility of the General Business Principles Review Committee, in close cooperation with Internal Audit.

The procedure for using the global violations database guides Compliance Officers and others (Human Resources Management, Internal Audit, Legal) in the registration and subsequent reporting (including escalation procedure, where applicable) of incidents brought to their attention. The rollout of the database started in June 2004, and as of July 1, 2004, new alleged violations will be entered in this database.

It is expected that this standardized form of reporting and escalation will not only provide a better and more transparent picture of the totality of alleged violations, but – due to the mandatory character of the system and the extensive network of compliance officers that each PD has set up for its major production sites – will reveal a larger number of alleged violations.

The Review Committee has developed a training program to accompany the introduction of the new standardized reporting system. This training program has been rolled

out throughout the world in close cooperation with the Regional and PD Compliance Officers.

To encourage reporting of GBP violations, we made further progress with the introduction of guaranteed-anonymity hotlines. These hotlines are now in place in the Philips organizations in North America, Latin America, a number of major European countries and virtually all of Asia Pacific. These hotlines can be telephone and/or e-mail.

#### Reported violations of the GBP

In total, 232 allegations were reported in 2004. A single allegation can relate to more than one type of (alleged) violations. As many of the allegations are currently still being investigated, it is impossible to determine exactly which – if any – General Business Principles have been infringed and to what extent. However, it is possible to draw some conclusions about those GBPs that are most frequently called into question.

GBP	Number of alleged violations per category	Percentage
4.3 Equal and fair treatment	70	26.1
6.1 Use and protection of assets	64	23.9
7.1 Bribery; records of transactions	54	20.1
7.2 Third-party interests	30	11.2
1 General commitment	17	6.3
6.2 Improper disclosure	8	3
1.3 Free market competition	8	3
4 Commitment towards employees	7	2.6
2 Commitment towards customers	5	1.9
4.2 Health and safety	2	0.7
1.4 Product safety	1	0.4
1.5 Privacy	1	0.4
3 Commitment towards shareholders	1	0.4

#### Risk assessment

End of 2004 it was decided to convert the present General Business Principles risk assessment tool into an instrument that can be used not only for risk evaluation and follow-up actions by the Review Committee, but also as an essential element of the control environment in the Philips anti-fraud program. For this it is necessary to identify not only the country risks, but also to expand its focus to specific product division/business-related risks and to ensure that the results of the analysis and evaluation are reflected in the company's audit program.

### Child labor

EIBE, the European Institute for Business Ethics of Nyenrode University, has completed a study of child labor in the supply chain. The aim was to underpin the development and implementation of a worldwide policy on child labor in Philips' supply chain. The results indicate that it is feasible to use a single basic approach to the implementation of a child labor policy for all countries. Insights derived from the study are being used to develop a blueprint for improvement plans.

This blueprint is intended to be part of the company's global child labor policy, and will set the basic approach for instances of child labor that are detected in the supply chain. Elements to be included in this blueprint are, among other things, the steps to be taken by Philips and its supplier, the involvement of civil society and governmental organizations, and standards for identifying the interests of the children. The blueprint improvement plan will be launched in the course of 2005 as an essential tool for Purchasing to use in follow-up actions with regard to a violation of the Supplier Declaration if child labor is detected in the supply chain.

### Human rights

For a discussion of how we are handling human rights, please see page 51.

# Sustainability at Philips

Sustainability offers a world of opportunities. At Philips we believe the way to explore these opportunities is by embedding sustainability throughout the organization, ensuring that it is an integral part of our strategic thinking and acting.

## Sustainability is a cornerstone of our strategy

More than 30 years ago, the Board of Management issued guidelines for environmental performance, followed by an environmental policy that was updated, keeping it a living document. Building on this firm foundation, the company developed its sustainability policy, which was released with the Sustainability Report 2002. (See page 90.)

We continue to be dedicated to sustainability, to finding the proper balance between the sometimes-competing demands of integrating social, environmental and economic responsibility. To do that, we are working to embed sustainability thinking in all of our day-to-day operations. This is our philosophy and a cornerstone in the strategy we have chosen to pursue.

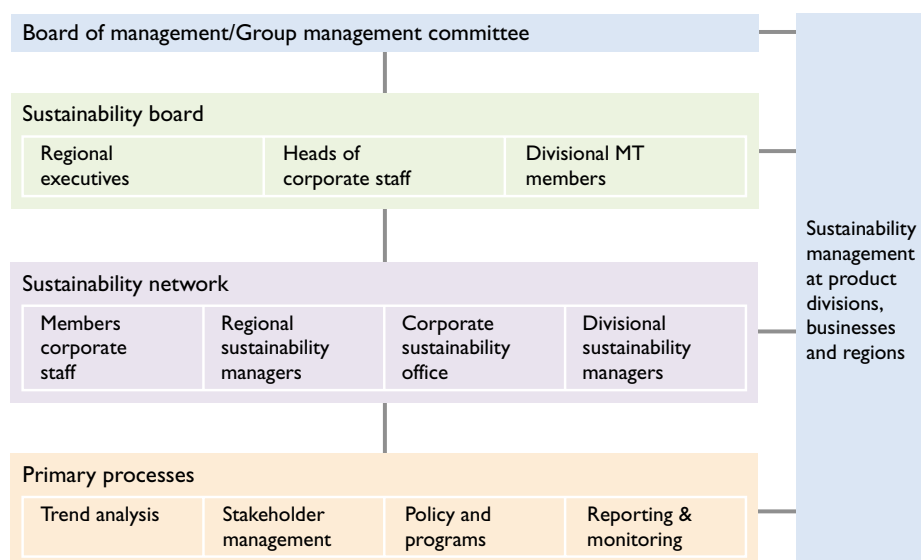
## Dow Jones Sustainability Index

For two years running we have been selected as the top company by the Dow Jones Sustainability Index (DJSI) World in corporate sustainability in the Cyclical Goods & Services market sector. This achievement is particularly rewarding and we will continue to work to improve our performance.

After being measured on our economic, environmental and social performance, our company was noted for strengthening its sustainability governance and vertically integrating sustainability management in product divisions, businesses and regions. The report said this has led Philips to respond to unique market challenges in developing countries.



## Embedded Governance Structure



The company's People Performance Management (PPM) appraisal process was deemed innovative for integrating corporate values by focusing on whether targets have been met and on how they have been achieved. Further, Dow Jones pointed to how we extended our sustainability commitment to suppliers by developing the Philips Supplier Declaration on Sustainability. Dow Jones also noted that our progress towards meeting ambitious eco-efficiency targets set under the environmental action program EcoVision is assessed through a comprehensive maturity grid, which includes sustainability elements.

The Dow Jones Sustainability Indexes track the financial performance of the leading sustainability-driven companies worldwide. Based on the cooperation of Dow Jones Indexes, STOXX Limited and SAM Group the indexes provide asset managers with reliable and objective benchmarks to manage sustainability portfolios. The Dow Jones Sustainability World Indexes (DJSI World) cover the top 10% of the biggest 2,500 companies in the Dow Jones World Index in terms of economic, environmental and social criteria. Philips ranked first among companies from the consumer electronics, leisure goods, home construction, apparel and airline sectors. Philips also came out on top in the DJSI STOXX<sup>SM</sup> index ranking of approximately 600 of Europe's leading companies.

Philips has been ranked top in sustainability among the companies on the Amsterdam Stock Exchange's AEX list of businesses in a survey conducted by Dutch Sustainability Research.

### WBCSD

Philips has been a member of the World Business Council for Sustainable Development (WBCSD) since 1993. The WBCSD is a coalition of 170 international companies united by a shared commitment to sustainable development via the three pillars of economic growth, ecological balance and social progress. Members are drawn from more than 35 countries and 20 major industrial sectors.

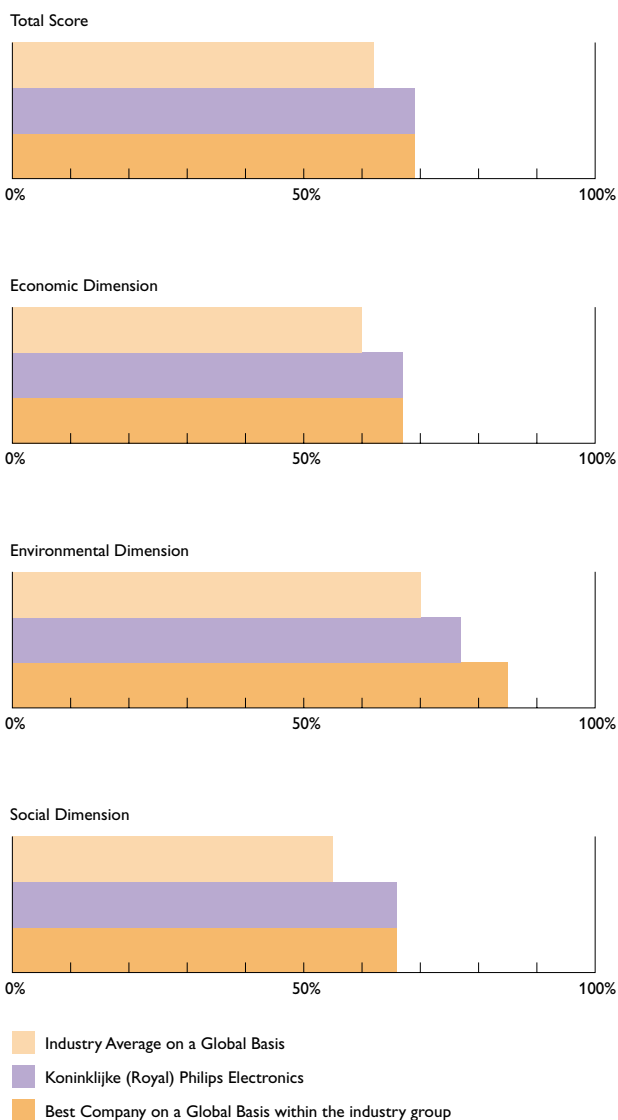


World Business Council for Sustainable Development

### Strengthened sustainability governance

As part of our ongoing efforts to strengthen our sustainability governance, in 2004 we established Regional Sustainability Councils in the Latin America and North America regions, chaired by their respective Regional Executive.

## Sustainability Scores – DJSI



At corporate level, the Philips Sustainability Board, which is chaired by a member of the Group Management Committee, includes a management team member from each of the product divisions, the regional executives, the CEO of Philips Research and the heads of Finance, Human Resources, Legal, Communications and Sustainability. Sustainability Directors at the product divisions support their management team members. These Directors report hierarchically to management level in their product division, and functionally to the head of the Corporate Sustainability Office, a Senior Vice President who is a member of the Sustainability Board.

The sustainability network also includes employees in nearly all functional areas, including communications, global brand management, finance, investor relations, purchasing, forwarding, human resource management, mergers and acquisitions, design, strategy, quality and research.

The Corporate Sustainability Office is responsible for trend analysis and benchmarking, providing guidance to the process of stakeholder management, preparing policy and action programs, monitoring and reporting and providing functional leadership to the divisional and regional Sustainability Directors. Cooperation with the divisional Sustainability Directors and employees from other functions, the Corporate Sustainability Office drives the execution of the company's sustainability action programs, and provides coordination at the Philips Group level.

#### Joint ventures and participations

Sustainability performance of joint ventures and participations where Philips has a minority stake or no operational control is being reviewed.

#### Embedding sustainability at Philips

To drive sustainability throughout the organization and involve all employees, Philips uses an embedded model approach. Based on external trend analysis and benchmarking results, improvement options or business opportunities are proposed. After discussions and management approval, implementation of defined programs is done via existing functional disciplines and business entities, with coordination and monitoring support provided at Philips group level.

This way of working applies both for the internal business system such as R&D, Product Development, Purchasing, Communications, Manufacturing and Services, as well as the extended business system consisting of suppliers and various other stakeholders including the financial community, customers, consumers, governmental and non-governmental organizations.

Following this model, we are working to firmly integrate sustainability throughout Philips – in the organization and company culture, in manufacturing and products, in the extended business system and in the company strategy.

#### Embedding in the company culture

Acting as a sustainable entrepreneur means stepping back and looking at what drives us as a company at the most basic level: our brand foundation, business strategy, values and expectations for business excellence. These core drivers form the basis for sustainable decision-making, which integrates economic prosperity, environmental quality and social equity.

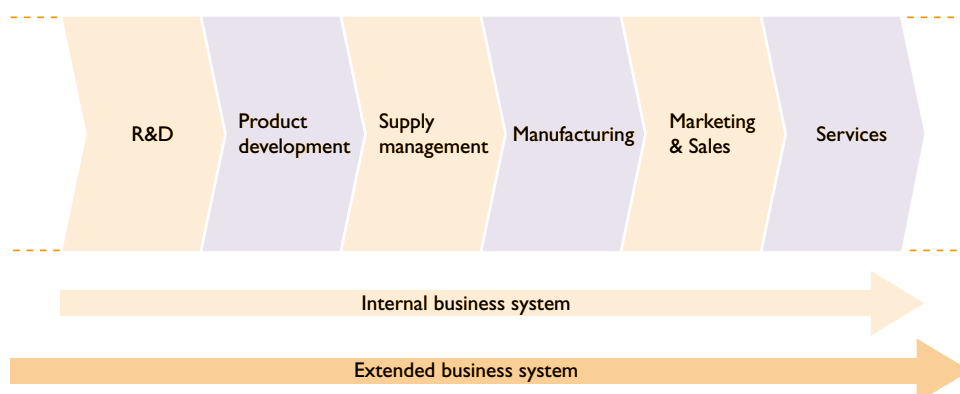
#### Embedding in manufacturing and products

In terms of its manufacturing processes, Philips has improved its environmental record, year in and year out, for more than three decades. To embed environmental responsibility throughout the organization, we began establishing coordinated, measurable action programs 10 years ago. In 1998, we launched our first EcoVision program, which called for the development of Green Flagship products. Today we have a portfolio of Green Flagships on the market. A selection is shown on pages 62-65.

#### Embedding in the extended business system

After years of being internally focused, companies must now broaden the scope outside their own organizations. This is critical in today's networked world where there is a growing interdependence on external parties.

### The Philips embedded model





To have a truly sustainable business, we also need sustainable suppliers. We started an extensive supplier involvement program in 2003. Our supplier program includes the Philips Supplier Declaration on Sustainability, which outlines the essential principles in the areas of environment, health and safety, and labor conditions, including child labor. (See page 100.)

We also recognized the need for intense dialogue with traditional and new stakeholders. (See page 20.)

#### Embedding in the company strategy

Philips mission is to improve people's quality of life, focusing on healthcare, lifestyle and technology. Our challenge lies in expanding our scope to new markets and new business opportunities with sustainability as a key driver. This includes new business models that will allow us to contribute in a meaningful and sustainable way to the quality of life of the 4 billion people at the world at the bottom of the economic pyramid, who earn less than US\$ 1500 a year. (See page 31.)

Key Performance Indicator (KPI)	
<b>Social</b>	
Health & Safety (1)	Level of presence
Health & Safety (2)	Number of Lost Workday injury Cases per year
Diversity & Inclusion	Percentage of women at executive level Percentage of Asians at executive level
<b>Business</b>	
New Business Initiative (1)	Number of projects
New Business Initiative (2)	Number of people that benefit from projects
Environment (energy use of products)	Number of Green Flagships with energy consumption as one of the focal areas
Supplier involvement	Application rate of Self Assessment tool by critical suppliers
<b>Communication</b>	
Reporting	Level of assurance
Stakeholder dialogue	Number of countries Philips management has a structured program in place
External communication	Number of favorable clippings in top 100 media
Internal communication	Sustainability messaging measured by Corporate Communications amongst employees

- risk and compliance management reporting
- our next environmental action program, EcoVision 2006-2009.

#### Driving our sustainability performance

We have incorporated standards into our management systems based on our strategy, stakeholder concerns and relevance to our business. These tools provide a necessary framework in the emerging area of non-financial reporting. To help us drive our sustainability performance, we have chosen the following tools: Global Reporting Initiative (GRI) Sustainability Reporting Guidelines, International Labour Organization (ILO) Core Conventions, ISO 14001 and International Standard on Assurance Engagements (ISAE 3000).

We believe that external verification is a vital part of our monitoring and reporting activities. It provides our stakeholders with assurance on the credibility and quality of our performance, and gives us valuable feedback for improving our processes and procedures. This is in keeping with our philosophy of continuous improvement.

By embedding sustainability we will move our organization:

From separate	To integrated
Operating in isolation	▶ Institutionalized throughout the organization
Many reports	▶ Integrated in the full business system
Scattered programs	▶ A coordinated approach
Internally focused	▶ Stakeholder involvement
Experienced as an add on	▶ Part of company strategy

#### Key Performance Indicators

For 2005 we have established a solid management agenda for sustainability and identified our first set of Key Performance Indicators at company level to track the progress of the major issues on our Sustainability Management Agenda. We will use these Key Performance Indicators to drive progress in the areas we deem important.

#### Sustainability Management Agenda

In addition to tracking our KPIs, the 2005 Sustainability Management Agenda looks at specific areas of interest for our company. Topics addressed include:

- labor indicators – working hours, HIV/AIDS, remuneration, collective bargaining, non discrimination, child and forced labor, training and education, attraction and retention

# Listening to our stakeholders

At Philips we strive to balance the often-competing demands of various constituencies. To understand the needs of our stakeholders, we are continuing to strengthen our approach to stakeholder dialogue. By listening to our internal and external stakeholders, we gain the information we need to help us effectively manage issues of importance to them and to our business.

We are working to create more structure around stakeholder interactions. The goal is to effectively manage resulting issues, as well as integrate stakeholder management into our business processes and procedures through the use of related KPIs.

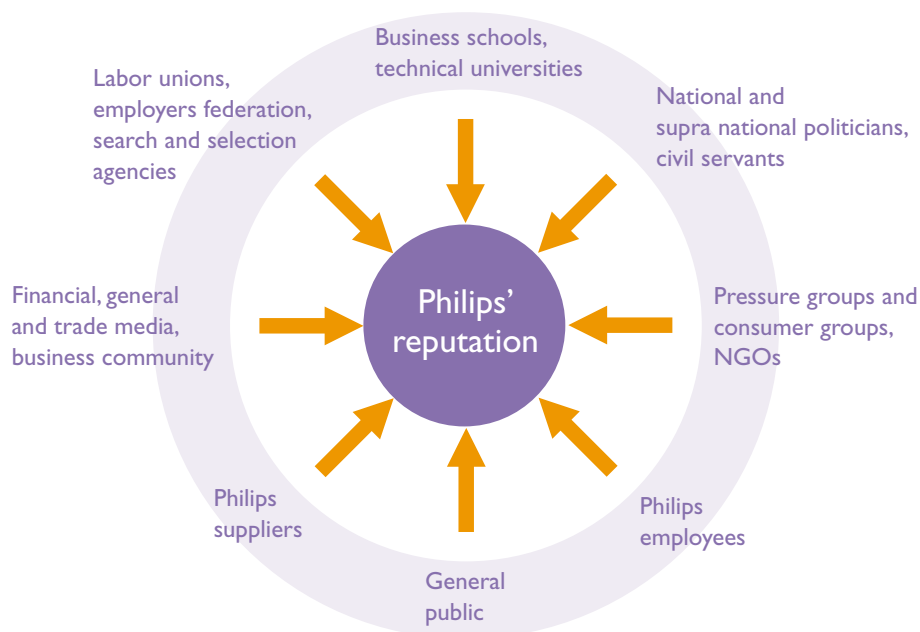
## Reputation research follow-up

To better understand stakeholders both inside and outside the company, Philips conducted a reputation study in 2003, consisting of interviews in eight countries around the world. We reported on the details of this research in the Philips Sustainability Report 2003.

During the course of 2004, we carefully evaluated the results and formed a Reputation Committee. Chaired by the CEO, the committee decided to focus on one key driver for reputation – performance management, improving our dialogue with all stakeholders on mission, vision and strategy. To drive implementation throughout the organization this effort is included in our business balanced scorecard for 2005.

Further, the results of the reputation research are being used around the company. For example, data from the survey has been valuable in supporting our decisions

## Opinion leaders



around our new brand positioning and brand promise. Knowing that many audiences want more information about our vision, and about Philips as a company, made it clear that the time was right to invest in a branding campaign.

### Our stakeholders

The chart below illustrates some of the ways we engage stakeholders. Examples of stakeholder engagement and feedback are included in the following pages of this section.

You will also hear from a variety of stakeholders throughout this report.

Stakeholder	Main means of interaction	Main Philips interface		
Economic stakeholders		Divisions	Countries/ Regions	Corporate
Customers	- (B2C) Surveys (trend related, customer satisfaction related, application research), complaint resolution. Focus groups, - (B2B) Advisory boards, co-R&D, co-strategy development	X	X	
Employees	Employee Engagement surveys, town hall meetings, People Performance mgmt system, compliance mgmt system, (local) ombudsman	X	X	X
Suppliers/business partners	Supplier days (local, global), co-R&D, industry membership (e.g., WBCSD)	X		
Mainstream investors	Road shows, analyst (face to face) meetings, ratings			X
Social investors	Surveys			X
Financial service providers	Ongoing ad hoc involvement, financial ratings			X
Social stakeholders				
Communities	Social investment activities focused on education and health, local networking		X	
Local/national/international regulatory bodies	Local networking (business/community driven). Participation in advisory bodies, cooperation in community projects		X	X
Non-governmental organizations	Surveys, project development, ad hoc involvement		X	X
Academia	Co-R&D, exchange programs, local networking		X	X
Media	Local networking, surveys	X	X	X

## Healthcare industry leadership

Frost & Sullivan presented five awards to Philips Medical Systems for technology and services innovation and industry leadership. Philips was selected after Frost & Sullivan conducted interviews with numerous market participants, customers and suppliers, along with extensive secondary and technology research. Manoj Kenkare, Vice President of Frost & Sullivan's Healthcare & Life Sciences Research Group, provides insight into the analysis behind the awards.



### How does Philips demonstrate its leadership in the healthcare industry?

**MK:** Philips has played an essential role in furthering a number of important trends in modernizing healthcare. With cutting edge technology development and deployment on the medical imaging, patient monitoring and health information technology fronts, Philips is clearly a leader in innovating not only the technology, but also the process and outcomes by which patient healthcare is administered worldwide. With today's race against time to provide high quality healthcare with limited resources, the means by which clinicians can access and utilize information has become critical.

### Some specifics?

**MK:** Philips' role in the industry could be summarized through the following examples:

- Looking at the healthcare IT segment, the Philips CompuRecord eliminates the need for manual intraoperative documentation by electronically integrating data from patient monitors, ventilators and anesthesia machines during surgery. This allows clinicians to concentrate on what's critically important, the patient, while still acquiring clear-cut documentation of vitals with no physical effort on their part.
- In diagnostic imaging, Philips has introduced a number of technologies targeted at improving medical outcomes while enhancing clinical workflow and efficiency. Products include the Panorama 1.0 T, the first open high-field MRI scanner with active shielding, the Brilliance

64-channel CT scanner, and the Eleve flat-panel cardiac and cardiovascular imaging system. The overall imperatives that guide Philips are the need to make diagnosis faster, maximize accuracy, minimize invasiveness, and provide value in the form of product quality, workflow enhancement and operational efficiency.

- From the perspective of external defibrillators and patient monitoring, Philips has been the earliest proponent of biphasic technology and has worked with leading medical associations to develop the necessary research methodologies to test the efficacy of using this technology. Since its adoption, biphasic technology has dramatically reduced or eliminated post-defibrillation heart dysfunction.

Frost & Sullivan credited Philips "for its ongoing commitment to public health as well as its public awareness campaign to educate the public about the importance of early access to defibrillation."

**MK:** Because of Philips' commitment to working with leading medical associations, legislators and the public, the adoption of automated external defibrillators (AEDs) is now becoming a standard first step to treatment of cardiac arrest in public facilities.

In the past, AEDs had only been available to individuals through a doctor's prescription and four hours of training. However, through its long time efforts and associations with the medical community, the Philips AED has become the first AED approved for over-the-

counter sales, enabling any individual to purchase such a device as a preventative measure. Philips' AED can be used by a layperson without any training. Advanced algorithms ensure that the device will only defibrillate if needed and has been proven many times over to be very reliable.

### What about future growth?

**MK:** The company's leadership position and its success within global markets will act as a tremendous catalyst for future growth within the healthcare industry. We believe this competitive edge enables a company like Philips to dedicate time and capital to such efforts as R&D, while peer firms struggle to keep their existing products afloat in very competitive markets. This ability to continue innovating and shaping healthcare practices may soon establish Philips as a hallmark by which operations in the industry are measured.

## Customers

Frost & Sullivan, a leader in growth consulting, presented five awards to Philips Medical Systems for technology and services innovation and industry leadership.

In announcing the awards in March 2004, Frost & Sullivan recognized Philips for making an outstanding contribution to the global cardiac resuscitation and medical imaging industries, and for establishing leadership across these markets.

## Employees

Philips India's Honeycomb initiative connects more than 4,000 employees spread over 35 locations and 10 businesses to make them feel engaged with and proud of the company, and make senior management open and accessible to employees.

Honeycomb won the First Prize in the Internal Communications category at Media magazine's Asia Pacific PR Awards Competition. And 'Let's Chat,' a core component of Honeycomb, was voted among the top six communications programs at the UK's Institute of Public Relations Excellence Awards. Awarding it first prize, the competition judges observed that Let's Chat was an excellent practical demonstration of the company's use of technology and one that demonstrated open and involved management.

## Suppliers

Philips held its first Global Supplier Forum in 2004. The event called Partners for Growth brought together the Philips Purchasing Leadership Board and 20 selected key strategic suppliers. It was intended to build closer relationships with the key strategic suppliers. During this one-day meeting in Amsterdam, President Gerard Kleisterlee and Ad Huijser, Chief Technology Officer, laid out the Philips strategic direction and the Research & Development roadmap.

Participants worked together on an action plan to develop a better and closer relationship to realize increased growth. Feedback from the suppliers was positive, varying from "excellent initiative" to "a very thought provoking meeting" and "extremely beneficial."

## Investors

The company is continuously striving to improve relations with its shareholders. In addition to communication with its shareholders at the Annual General Meeting of Shareholders, Philips elaborates its financial results during (public) conference calls, which are broadly accessible. It publishes informative annual and quarterly reports and

press releases, and informs investors via its extensive website. The company is strict on its compliance with applicable rules and regulations on fair and non-selective disclosure and equal treatment of shareholders.

Each year the company organizes major Philips Product Divisional analysts days and participates in several broker conferences, announced in advance on the company's website and by means of press releases. Shareholders can follow in real time the meetings and presentations, organized by the company, by means of webcasting or telephone lines. It is our policy to post presentations to analysts and shareholders on the company's website. These meetings and presentations will not take place shortly before the publication of annual and quarterly financial information.

In November 2004, IR Magazine voted Philips one of the top five Eurozone companies for the quality of its investor relations.



Our first Global Supplier Forum was designed to build closer relationships with key strategic suppliers.

## Governments and NGOs

Examples of our work with various government agencies are discussed throughout this report. In the following pages you will read about our work with governmental and non-governmental organizations (NGOs) on such issues as privacy, unemployment and take-back and recycling, as well as on our social investment projects. As part of our new business initiative, discussed in the section titled 'Our strategic direction,' we provide details of how we are working with governmental and non-governmental organizations to explore new business models with sustainability as a key driver. This is pioneering work that is providing extensive learning to all parties.

# Our strategic direction

In the next 50 years, world population will increase from today's 6 billion to between 9 and 11 billion.

Material consumption will grow substantially, putting additional strains on limited resources, thus demanding technological innovation.

## Our perspective

As the population increases the needs of people in advanced markets, and even more so in developing and emerging markets, can provide significant potential for business. To succeed, business has to understand the nature of change and respond to people's desire for improved quality of life.

It is our firm belief that socially and environmentally responsible behavior contributes to sustained profitable growth and value creation. That's why we are embedding sustainability thinking and acting in all of our daily activities. This is our philosophy and a cornerstone of our strategy.



## Trend analysis

Understanding the bigger picture – and keeping it top-of-mind – affords a clear horizon for long-term. To gain that perspective we review the latest analyses from a variety of sources, including the World Bank, World Business Council for Sustainable Development, World Summit in Johannesburg and World Economic Forum, as well as our own research.

With this as a starting point, we consider medium-term societal trends, focusing on those issues that mirror our core competencies. It's about forging strong links between our commitment to improve quality of life as a leading solutions provider in the areas of healthcare, lifestyle and

## Our mission

We improve the quality of people's lives through the timely introduction of meaningful technological innovations.

## Our vision

In a world where technology increasingly touches every aspect of our daily lives, we will be a leading solutions provider in the areas of healthcare, lifestyle and enabling technology, aspiring to become the most admired company in our industry as seen by our stakeholders.

## Our strategy

We will:

- increase profitability through re-allocation of resources towards opportunities offering more consistent and higher returns
- leverage the Philips brand and our core competencies in healthcare, lifestyle and technology to grow in selected categories and geographies
- build partnerships with key customers and suppliers, both in the business-to-business and business-to-consumer areas
- continue to invest in maintaining world-class innovation and leverage our strong IP position
- strengthen our leadership competencies
- drive productivity through business transformation and operational excellence

## Our values

Delight customers  
Deliver on commitments  
Develop people  
Depend on each other



Subject	Trends	Issues	Philips strategic response
Demographics	<ul style="list-style-type: none"> <li>Growing population with an increasing demand for improved quality of life</li> </ul>	<ul style="list-style-type: none"> <li>Clean water and sanitation</li> <li>Health and communicable diseases</li> <li>Climate change (global warming)</li> <li>Limited resources (energy, materials)</li> <li>Education</li> <li>Eradication of poverty</li> </ul>	<ul style="list-style-type: none"> <li>Focus on healthcare products</li> <li>Social investment program focused on health</li> <li>EcoVision program</li> <li>EcoDesign of products with weight, energy reduction and recyclability as focal areas</li> <li>Social investment program focused on education</li> <li>Pilots in new and emerging markets with sustainability as business driver</li> </ul>
	<ul style="list-style-type: none"> <li>Aging population with an increasing demand for improved quality of life</li> </ul>	<ul style="list-style-type: none"> <li>Focus on early identification of diseases and treatment</li> <li>Expanding costs for healthcare</li> </ul>	<ul style="list-style-type: none"> <li>Preventive healthcare products</li> <li>Personal healthcare products</li> </ul>
Society	<ul style="list-style-type: none"> <li>Retreating governments</li> <li>Emerging role of industries and NGOs (non-governmental organizations)</li> </ul>	<ul style="list-style-type: none"> <li>Limited supranational regulations</li> </ul>	<ul style="list-style-type: none"> <li>Stakeholder dialogue</li> <li>NGOs and governments as business partners</li> <li>Active role in WBCSD, GRI, UNEP, etc.</li> </ul>
	<ul style="list-style-type: none"> <li>Demand for reduction of hazardous substances in products</li> <li>Waste reduction</li> </ul>	<ul style="list-style-type: none"> <li>Lead-free soldering</li> <li>Mercury reduction</li> <li>Take-back of electronic products</li> </ul>	<ul style="list-style-type: none"> <li>Lead-free soldering program</li> <li>EcoDesign with hazardous substances as focal area</li> <li>Active role and participation in recycling programs</li> </ul>
	<ul style="list-style-type: none"> <li>Demand for a decrease in complexity</li> </ul>	<ul style="list-style-type: none"> <li>Complicated use of electronic products</li> </ul>	<ul style="list-style-type: none"> <li>Focus on simplicity of products underlined by Sense and Simplicity brand promise</li> </ul>
	<ul style="list-style-type: none"> <li>Rising attention for human rights</li> </ul>	<ul style="list-style-type: none"> <li>Demand for transparency</li> </ul>	<ul style="list-style-type: none"> <li>General Business Principles</li> <li>Supplier Sustainability Program</li> </ul>
	<ul style="list-style-type: none"> <li>Demand for security</li> </ul>	<ul style="list-style-type: none"> <li>Dealing with privacy</li> </ul>	<ul style="list-style-type: none"> <li>RFID business development</li> <li>Privacy policy</li> <li>Lighting as security application</li> </ul>
	<ul style="list-style-type: none"> <li>Increase of on- and off-line electronic communication, both in advanced and emerging markets</li> </ul>	<ul style="list-style-type: none"> <li>Changing business models</li> </ul>	<ul style="list-style-type: none"> <li>Joint ventures and partnerships</li> <li>NGOs, academia and governments as business partners</li> <li>Connected Planet approach</li> </ul>
	<ul style="list-style-type: none"> <li>Increase of accountability</li> </ul>	<ul style="list-style-type: none"> <li>Product safety</li> <li>Employee health and safety</li> </ul>	<ul style="list-style-type: none"> <li>Global product safety policy</li> <li>Global health and safety reporting system</li> </ul>
	<ul style="list-style-type: none"> <li>Spread of AIDS/HIV</li> </ul>	<ul style="list-style-type: none"> <li>Increasing uncertainty</li> <li>Strong impact on quality of life in developing countries</li> </ul>	<ul style="list-style-type: none"> <li>General Business Principles</li> <li>Policy development for employees</li> <li>Social investment program in communities focused on health and education</li> </ul>
Consumer behavior	<ul style="list-style-type: none"> <li>Shift from product to experience</li> <li>Demand for improved quality of life</li> <li>Individualization and diversification</li> </ul>	<ul style="list-style-type: none"> <li>Identification of consumer needs in advanced and emerging markets</li> </ul>	<ul style="list-style-type: none"> <li>Focus on lifestyle products</li> <li>Focus on healthcare products</li> <li>Sustainability as business driver</li> <li>Diversity and inclusion initiatives</li> </ul>
Technology	<ul style="list-style-type: none"> <li>Miniaturization and function integration</li> <li>Emerging new technologies (LED, nanotechnology, molecular imaging, water purification, hydrogen energy)</li> <li>Increase of importance of services</li> </ul>	<ul style="list-style-type: none"> <li>Protection of intellectual properties and pay-back of research investments</li> <li>Standardization</li> <li>Changing business models</li> </ul>	<ul style="list-style-type: none"> <li>Selection and focus on key technologies</li> <li>Continuous review of strategic portfolio</li> <li>Joint ventures and partnerships</li> <li>Sustainability as business driver</li> </ul>
Business	<ul style="list-style-type: none"> <li>Global markets</li> <li>Increasing economic power in Asia-Pacific</li> <li>Consolidation and integration of industries</li> <li>Intensified price competition</li> <li>High-speed innovation</li> <li>Outsourcing of production to low-wage countries</li> <li>Focus on know-how management</li> <li>New and emerging markets</li> </ul>	<ul style="list-style-type: none"> <li>Effective supply management is pre-condition</li> <li>Employability</li> <li>Knowledge transfer</li> <li>Protection of intellectual properties</li> <li>Partnerships</li> <li>Industrial re-allocation</li> </ul>	<ul style="list-style-type: none"> <li>Supplier Sustainability Program</li> <li>General Business Principles</li> <li>Intellectual property/know-how management</li> <li>Joint ventures and partnerships</li> <li>NGOs, academia and governments as possible business partners</li> <li>Responsible transformation in Europe, position paper</li> <li>Pilots in new and emerging markets with sustainability as business driver</li> </ul>

technology – and doing that in a way that is consistent with our philosophy and values.

The chart on the previous page outlines trends and issues with particular relevance for our company, along with our strategic response. You will find examples of how we turn our strategy into action in this section and throughout this report.

### Sense and simplicity

The need to simplify the way we experience technology is a trend we recognized and wanted to address. Customers in the healthcare, lifestyle and enabling technology markets that Philips operates in want common sense from the company: systems that are clever yet logical and adaptable to their future needs, solutions that are elegant yet straightforward, components that are smart yet simple. Plus, they want to do business with the company in a sensible and simple way.

‘Sense and simplicity’ is much more than just our brand promise – it’s at the heart of our company. We are committed to delivering products and solutions that are ‘designed around you,’ ‘easy to experience’ and ‘advanced.’

### Healthcare

At Philips our healthcare activities traditionally have been focused in the business-to-business field, but we are increasingly applying our expertise to the consumer health and wellness market. Whether we are developing solutions



Technology should be as simple as the box it comes in.

for hospitals and doctors, or for the growing number of health-conscious consumers, Philips is committed to bringing innovative solutions to the market that will set the standard for future healthcare.

### The friendlier hospital

A hospital visit can be a cold, impersonal event. We think this perception can be changed. By cleverly combining lighting, electronics and medical systems with award-winning design, the Philips Ambient Experience can transform the hospital environment.

Harsh fluorescent lights are replaced by lighting mimicking nature’s rhythms. The clinical environment is softer too,



We use an innovative human-focused approach – the Philips Ambient Experience – to improve the experience of patients and clinicians who work with our medical equipment.

# Tapping the trends

In line with Philips' commitment to driving growth and profitability by focusing on healthcare, lifestyle and technology, 2004 saw the creation of an exciting new DAP business unit, Consumer Health & Wellness. Ivo Lurvink, the unit's General Manager, explains what it's all about.



## From hospitals to homes

Research shows that healthcare is gradually moving out of the hospital and into the home, as consumers increasingly focus on their personal wellbeing, and demand more say over how and where they manage their health issues and receive treatment. At the same time, the aging population is faced with a growing number of chronic yet manageable conditions, such as obesity, cardiovascular disease and diabetes. Yet another factor is the high and ever-rising cost of hospital care, which on average is as much as 10 times higher than treatment at home.

All together, this makes a compelling business case for simple, effective products consumers can use to monitor their overall health and wellness themselves, without having to consult a medical professional, or to treat themselves or others in an emergency. That's exactly what Consumer Health & Wellness aims to provide.

## Strong foundation

Philips has already had success in this field, with HeartStart Home Defibrillator, a simple, easy-to-use defibrillator that can be used at home, at work or on the go to save lives, providing the user with clear instructions on how to operate the device. Another example is Philips Heartcare Telemedicine Services, launched in Europe in 2001, which provides cardiac monitoring over a telephone line to a medical call center.

Moreover, the company is ideally placed to become a key player in this sector, as Lurvink explains. "Philips already has the necessary competences for this sector in house. On the one hand, Medical Systems has a wealth of expertise in developing healthcare systems that are exceptionally efficient and cost-effective. On the other, DAP has in-depth consumer insights and vast experience in translating technology and professional

knowledge into user-friendly solutions for the home. Consumer Health & Wellness will combine and capitalize upon both of these core strengths, giving us a key competitive advantage."

In short, the unit will develop and market products that meet both the 'sense and simplicity' requirements for the Philips brand.

## Preparing for success

The unit has ambitious goals, Lurvink says. "In 2005, we'll be focusing on making sure all the pieces are in place. First and foremost, this means having the right people, with the right skills, vision and passion for this exciting venture. Fortunately, because this sector is so relevant to each and every one of us, that passion is relatively easy to find."

with a changing room that resembles a comfortable hotel. Your own 'smart card' holds your personal preferences so when you enter the exam room the card triggers your pre-selected atmosphere. The walls and ceiling come alive with comforting sounds and images of the patient's choice – from nature and meditative scenes even to cartoon characters.

The Ambient Experience is not just a concept. Advocate Lutheran General Children's Hospital in Park Ridge, Illinois, US, is constructing a pediatric computed tomography (CT) suite based on these principles.

## Lifestyle

People are at the heart of our activities. We are focused on enhancing convenience, pleasure, safety and health – at home and on the move – with innovative products designed to make your life more simple.

## Enlightened lighting

Philips refurbished the Eiffel Tower's lighting system with energy saving EcoDesigned lamps. In addition to replacing the 352 existing Philips projectors that equipped the Eiffel Tower for the last 18 years, the new lighting saves at least 30% in energy consumption and the team reduced the dimensions of the spotlight equipment by 50%.

The lighting also conforms to new security regulations and operating conditions, which include exceptional vibrations and wind-speeds over 180 kilometers per hour. Plus, the new projector bulbs had to offer the same luminosity ratings as the earlier lamps.

Philips created a line of new generation energy-saving light bulbs, which helped to preserve the visual impact of the Paris landmark at night, while saving 40% on operating costs.



#### Experiencing TV in a new light

Ambilight is a unique feature from Philips that provides ambient light onto the wall surrounding the television. Viewing TV in a darkened room, even for short periods, can cause eyestrain. This is because of the continuous adjustments that your eye must make as scenes change from dark to light.

Providing a complementary light behind the set alleviates these extreme adjustments, resulting in more relaxed viewing. By eliminating eyestrain, your eye is able to see more. Significant improvements in perception of contrast, black level and detail are enabled through Ambilight.

#### Technology

Being able to work on the frontiers of science and ideas into innovations that improve people's lives is in keeping with the spirit of discovery our company has long nurtured.

#### OLED displays

Our scientists have developed new methods to significantly increase the efficiency of PolyLED polymer OLED (organic light-emitting diode) displays. This opens the way to lower power consumption and will further strengthen the inherent advantages of polymer OLED for mobile and other applications, namely high brightness and contrast, wide viewing angle and excellent video capabilities, but

also enables the use of polymer OLEDs in solid-state lighting applications. Higher efficiency allows low-cost, large-scale manufacturing of OLEDs, which are expected to evolve into a truly powerful display technology capable of rivaling LCDs.

#### Handshake solutions

Handshake Solutions is a Line of Business in the Philips Technology Incubator marketing a clock-less design for microprocessors that dramatically reduces power consumption and electromagnetic emission of digital systems. In October 2004, Handshake Solutions and ARM announced a joint development and marketing of an ARM® processor using the Handshake Solutions unique low-power, self-timed technology.

The key benefits of the processor include low electromagnetic emission, which decreases the probability of interfering with sensitive circuitry, and low peak currents, which reduces system power requirements. Because asynchronous processors consume zero dynamic power when there is no activity, they can significantly extend battery life. The new ARM processor will be available as a licensable product from ARM in the first quarter of 2005.

#### Key issues and opportunities

To meet the challenges ahead, global enterprises need to work differently. At Philips we have been working to create a simpler, more responsive organization. Speed and innovation are essential to succeed in an increasingly competitive marketplace.

Our ongoing transformation will be supported by an increasing network of joint ventures, partnerships and alliances with third parties that provide expert knowledge to bring new business models to market, maximizing the value of investments in technology.

Such change raises issues and offers opportunities for us to explore. The following pages highlight some of these areas, including intellectual property rights, open innovation and partnerships.

#### Intellectual property rights

Supporting countries with emerging economies deal with the issues around intellectual property rights (IPR) will be one of the major business challenges of the 21st century. Recent initiatives involving Philips and the Chinese authorities may provide a blueprint for the future by showing how companies and countries can work together for their mutual benefit.

Philips investments in China in both manufacturing and research demand a solid intellectual property system to secure inventions, models and brands. China also needs a solid IPR system to secure its local innovation and be attractive for foreign investors. To make this a reality, Philips works closely with Chinese government officials to create awareness of IPR among consumers and industry.

We have established an IP Academy at two of the most prestigious universities in Beijing, Renmin and Tsinghua, and in Fudan in Shanghai, providing and exchanging IP experts

and sponsoring IP research. Further, we participate in Chinese efforts on standardization in the field of communication and entertainment systems, through close cooperation with local standardization bodies, like the China Communication Standards Association, as well as local and international technology partners.

## Sharing our IPR expertise

“Working closely with the authorities builds mutual respect and ultimately benefits everyone involved by giving a boost to the development of local knowledge, locally developed technology and local IPR,” explains Azir Haque of the Philips Intellectual Property & Standards’ China office.



With 15 R&D centers employing hundreds of Chinese people, there are more than 200 ‘Made in China’ Philips patents so far. And the company’s strategic R&D for Asia Pacific will be centered at the Philips Research laboratory in Shanghai.

Then there is Open Innovation. As a result of Open Innovation, more and more Chinese companies are tapping into Philips’ knowledge, especially in consumer electronics. For example, more than 100 companies have taken out licenses to use Philips patents to produce DVD players.

### Building mutual respect

“Good IPR stimulates direct investment by foreign companies and enables technology transfer and R&D cooperation,” says Haque. “What you get is a virtuous circle of transfer of foreign IPR and generation of local IPR. Countries that want to develop their own technology need their own IPR, and that translates into respect for the IPR of others. This is what we see happening in China now.

In the end, this will create a level playing field between local and foreign companies.”

Philips runs workshops to educate and build up local IP expertise resources. We have excellent cooperation from the authorities and we hold regular meetings to solve practical problems. Further, the Chinese authorities have been working to build up a complete IPR framework.

### IP Academy

To provide practical assistance, we created the IP Academy. “This is going to offer us the long-term solution,” he says. “If we educate a hundred people on IP issues, they are going to tell a hundred more, and so on. The effect is unimaginable in scope. And that’s how you reach every strata of society in a country as big as China.” Established around the law faculties at Fudan, Renmin and Tsinghua, the Academy itself follows guidelines of European IP law. Philips IP&S experts worked with Chinese professors to amend the curriculum in line with Chinese needs. Student

scholarships and an exchange program for Chinese professors to visit the US or Europe to further develop additional IP skills are part of the Academy program. So too is a substantial budget for IP-related research, with the university proposing ideas and Philips providing the funds.

### Local benefits

We believe that the initiative will not only result in a more level playing field for Philips and other investors, but that it will also benefit Chinese-owned businesses. This is because further improving the country’s IPR protection will encourage Chinese companies to innovate, which, in turn, will improve the country’s overall competitiveness.

“The IP Academy is part of our pledge to support China as it develops its own technology base, a base that will aid the country’s overall evolution and will benefit everyone involved down the road,” Haque says.



### Open Innovation

Philips currently holds 115,000 patent rights, 22,000 trademark registrations, 6,000 design rights, and 2,000 domain name registrations. With its 2004 filing of more than 3,000 patents, Philips is first on the World Intellectual Property Organization (WIPO) ranking in new patents for the third consecutive year.

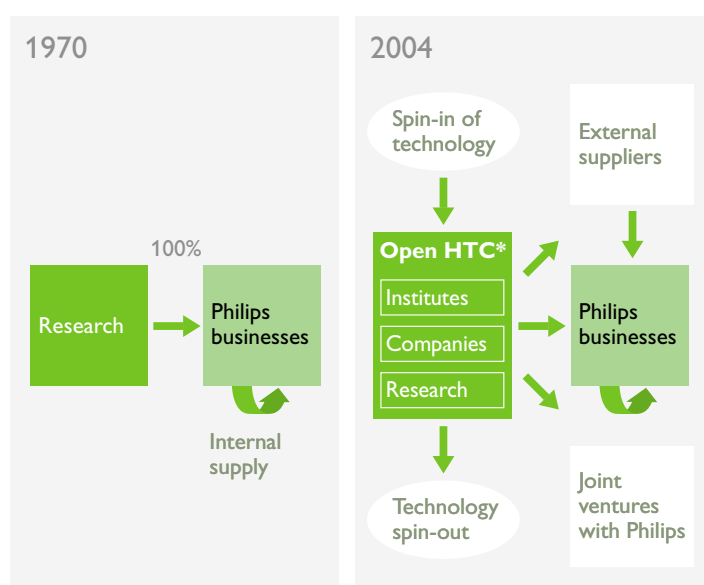
This portfolio is not the result of in-house innovation only. At Philips we have adopted Open Innovation as our method of working. That means we team up with academic and industrial partners who have competencies and interests complementary to our own, join forces with industry peers on standardization and create momentum in the future directions of technology we jointly aspire to, and are active in establishing strong local networks of leading industries and research institutes that help top technology regions to grow. The percentage of Philips Research projects carried out in cooperation with a university or non-governmental organization has increased to approximately 55% in 2004, from 47% in 2003.

Many factors have necessitated this change in innovation approach. The increased mobility of the technical workforce, increasing high quality university research, emerging start ups that pull ideas and people out of corporate and university labs, along with the increasingly global character of markets, mean that great ideas and technologies can arise from anywhere in the world.

The concept of Open Innovation is a radical departure from the traditional model of closed, in-house innovation. The key is for innovators to keep searching not only inside but also outside the company for the next revolutionary idea. The researcher behind a new patent becomes as valuable as the researcher who spots a discovery outside the company and adopts it for use in-house.

Perhaps the clearest proof of our commitment to Open Innovation is the Philips High Tech Campus in Eindhoven,

### From 'internal' to 'open innovation'



\* HTC = High Tech Campus

## Distance Learning

Open Innovation can serve society in such areas as education. Distance learning in China is a key element in serving the educational needs of a widespread and often remote community. As such, it receives significant regional and national support, as well as government funding. However, distance learning in China is currently fragmented and often based on less-than-ideal, yet high-cost solutions.

The answer is a system developed in China to meet the specific needs of its people and one that is based on open standards. The functionality required at the user end is a means of recording and replaying interactive content at cost levels significantly below that of a PC, making Philips' personal video recorder and set top-box capabilities a natural fit.

To provide the expertise required for program delivery and authoring, Philips teamed up with a leading Chinese distance-learning company. On the Philips side, providing the required technological solution has been a true One Philips approach, bringing in Consumer Electronics to provide system-level support and testing, Semiconductors for product management and reference design creation, and the Digital System Labs for architecture and software integration management. Philips Research East Asia in Shanghai handled pre-commercialization aspects, including the forging of links with Chinese government departments, participation in standardization groups and a significant amount of IP generation.





## Partnership makes an impact

Amandus Lundqvist, President of Eindhoven University of Technology, talks about partnering with Philips.

A delegation led by Rick Harwig, CEO of Philips Research, and Amandus Lundqvist, President of Eindhoven University of Technology, visited four top universities in China to investigate opportunities for cooperation between the respective research institutes. The delegation visited Tsinghua University in Beijing, Zhejiang University in Hangzhou, and Fudan and Jiaotong in Shanghai, all listed in the top 10 of the China College and University Rankings 2004.

Establishing cooperative relationships offers unique opportunities for all parties to further strengthen their Chinese-European collaboration in a joint industrial and academic setting. The Philips and Eindhoven University of Technology approach brings a fresh perspective to this type of effort.

"The ten best Chinese universities have businesses coming to them all the time, and other universities also want to work with them," says Lundqvist. "But it's rare that a corporation and an academic institution go together with proposals to work on specific topics. A joint delegation like ours makes a different impact. Having a strong partnership with a company shows how you are going to apply the knowledge you are developing."

Several types of cooperation include staff-exchange programs, joint education initiatives and joint R&D projects. As a result of the delegation's visit, Chinese students are working and studying in Eindhoven, the Netherlands.

"This type of public-private partnership is very valuable," Lundqvist notes. "It's interesting for all the partners and is something that will grow and evolve over time. To make these relationships truly work, you have to have a long-term vision."

the Netherlands. Companies are encouraged to make use of both the infrastructure and the considerable expertise and experience available to them at the facility.

The Philips Microsystems Plaza (MiPlaza) opened on the campus in June 2004 with facilities for innovation in materials, devices and Microsystems. More than 150 Philips researchers work at MiPlaza side by side with their counterparts from other companies, universities and other research institutes. The MiPlaza cleanroom ranks as one of the largest multi-purpose research cleanrooms in the world.

Another example of pre-competitive cooperation is the Crolles2 R&D Center near Grenoble, France. This joint venture by Philips, Motorola and STMicroelectronics is unprecedented in the microelectronics industry. The research conducted at the facility is pushing forward the frontiers of semiconductor technology.

### Exploring new business opportunities

To meet the needs of people around the world, Philips has challenged its employees to explore new business opportunities and new markets with sustainability as a key driver. We have asked employees to develop a business case for projects in advanced, emerging and developing markets that will benefit people and contribute to our growth.

During 2004 we launched a pilot in Brazil and laid the groundwork for another in India. We have worked to nurture relationships and strengthen partnerships with NGOs, governments, other companies and more. To drive that process we have conducted four workshops. Of the many ideas that were proposed, two have been selected for further investigation.

In 2005 we will work to speed up this process and drive it through the organization, engaging cross-functional teams from R&D, the regions and product divisions.

### Voices in Your Hand

Our Voices in Your Hand is a pilot project running in Recife, Brazil, to bring digital connectivity to people at the bottom of the economic pyramid. With Voices in Your Hand, people in this underserved community – many are illiterate – can communicate with others and have access to information even though fixed-line or wireless phones are beyond their economic reach.

Using modified MP3 players, people can listen to personalized web casts of audio information offline in their homes, talk



# Driving Innovation from the Base of the Pyramid

By Stuart L. Hart

Stuart L. Hart is currently SC Johnson Chair of Sustainable Global Enterprise and Professor of Management at Cornell's Johnson Graduate School of Management. He is the author of *Capitalism at the Crossroads: The Unlimited Business Opportunities in Solving the World's Most Difficult Problems*.

More than 4 billion people – fully two-thirds of humanity – at the base of the economic pyramid are subsistence oriented and satisfy their basic needs directly from nature, participating only sparingly in the money or formal economy. Demographers generally agree that as the world's population increases during the next few decades, most of the growth will occur in these markets, which are dominated by the poverty and isolation found in the rural villages of the developing world.

## Unprecedented business opportunity

Because vibrant small communities in rural areas stem the pressure for mass migration and accompanying social, political and environmental breakdown, focusing on this market is both the key to sustainable development and an unprecedented business opportunity for visionary firms. Managers can identify sustainability-related opportunities by asking these questions:

- Can our existing products and services be modified to meet the needs of the poor?
- Can we apply state-of-the-art sustainable technology to meet the needs of those at the base of the economic pyramid?
- Have we overlooked market vacuums, where needs are fundamentally unmet?
- Are we blinded by our current business model?
- Can we build a customer base that can become more substantial over time?

## Meeting real need

Companies need to focus on technologies, products and services geared specifically to the needs of those at the base of the economic pyramid. Managers must understand four factors:

- Deep listening and mutual learning are necessary if products and services are to meet real needs.

- Significant profits can be realized by meeting the needs of the poor and disenfranchised.
- Meeting those needs offers the opportunity to apply state-of-the-art (sustainable) technology in fundamentally new ways. Simply transplanting business models from the consumer or even emerging markets will not work.
- Business models must leverage local talent, create employment opportunities and build capacity in the local community.

To succeed it is crucial to develop a vision not only for what needs the company is trying to address and how they relate to sustainability, but also where the most appropriate markets can be found. The unmet needs of those at the base of the economic pyramid may present the best opportunity for firms to define a compelling trajectory for future growth and innovation.

## A new mindset

Doing business this way requires multinational corporations (MNCs) to re-evaluate price-performance relationships for products and services. It also demands a new level of capital efficiency and new ways of measuring financial success. Companies will be forced to transform their understanding of scale from 'bigger is better' to highly distributed small-scale operations married to world-scale capabilities.

For boards, senior executives and business leaders with the audacity and desire to compete at the base of the world economic pyramid, the prospective rewards include growth, profits and incalculable contributions to humankind. Furthermore, MNCs' investment at the base of the pyramid means lifting billions of people out of poverty and desperation – and averting the social decay, political chaos, terrorism and environmental meltdown that is certain to result if the gap between rich and poor continues to grow.

back and use voice email. Then they visit a public utility point to link their sets to the Internet. The customer here may be a family or a village, rather than an individual.

During 2004 we conducted extensive market research as well as a social impact survey. We have developed partnerships to supply content and Internet service and distribute handsets to the potential users. In November the rollout started providing 10 handsets per week to a representative group of users in the community of Chão de Estrelas, and plan to have distributed a total of 250 handsets by March 2005. Each handset can have multiple users and the pilot targets a level of approximately 500 users.

The pilot will be completed mid 2005, learning will be captured and results will be used to test the feasibility of possible scale up scenarios.



Our Voices in Your Hand pilot brings Internet content to an underserved community in Brazil. Voices in Your Hand brings digital connectivity, allowing people to communicate with others and have access to information.



## Partnerships are the key

Marcos Magalhaes, Regional Executive for Philips Latin America, and Serguem Silva, National Director of World Vision in Brazil, one of the partners involved in the Voices in Your Hand project, talk about the collaborative relationships necessary to bring new business models to people at the base of the economic pyramid.

Exploring new sustainable business opportunities like the Voices in Your Hand pilot in Brazil involves a shift from a business-as-usual mindset. "To be successful we must nurture collaborative relationships with a multitude of stakeholders like non-governmental organizations, governments, universities, communities, other companies and so on," says Marcos Magalhaes, Regional Executive for Philips Latin America.

"Under the traditional model, companies simply gave money to various organizations that then worked on their own. Our new business model with sustainability as the driver founded on the ethics of co-responsibility requires true partnership, with buy-in and understanding. And, as with any relationship, there must be mutual respect and trust," he stresses. "This means each party must see things through their partner's 'filters.' It's about realizing that we're dealing with different perceptions, concepts and belief however keeping in mind

that all the efforts must come to the ultimate benefit of our target group, namely people at the base of the economic pyramid."

### Searching for solutions

Establishing these relationships was essential to lay the foundation necessary for this pilot. Serguem Silva, National Director of World Vision in Brazil, one of the partners involved in the Voices in Your Hand project, explains that this approach historically has not been the norm. "Regretably, most people searching for solutions to social problems worked in isolation. For a long time there was a certain fear of cooperations between corporations and non-governmental organizations – not only because of the difference in focus but also because of preconceived notions on both sides," he says.

The good news is that this is changing. "World Vision's experience with Philips and Voices in Your Hand shows that by joining experience

and knowledge in distinct fields, working in a complementary way, it's possible to make an extraordinary difference in making the world more inclusive," Silva notes.

### Making an impact

As a relief and development organization dedicated to helping children and their communities worldwide reach their full potential by tackling the causes of poverty, World Vision sees this project as an example of using NGO experience to make a high social and economic impact on people living in poverty, according to Silva. "This is really social responsibility," he says.

Magalhaes agrees. "This pilot represents much more than just a significant business opportunity. By helping to give digital access to underprivileged communities, Philips and our partners can make a real difference in people's lives."

With our DISHA pilot, we aim to bring healthcare to the people who are not addressed by the existing healthcare system like these villagers in Tamil Nadu, India.



### DISHA

Philips India has developed a business plan for providing distance healthcare for the underserved people at the base of the economic pyramid. Called DISHA (Distance Healthcare Advancement), the goal of this initiative is to deliver high quality, low cost diagnostics to those who are not addressed by the existing healthcare system.

In 2004 the company conducted research in target communities to determine the proper delivery model. The research revealed the fact that people with lower incomes spend a higher proportion on healthcare than those in higher income levels. A high large percentage of those costs go to paying high interest rates on loans for healthcare, with the rest to account for travel and lost work time. Research also helped the company narrow the scope of the project to focus on two key areas: mother and child, and trauma.

We formed partnerships to bring the DISHA vision to life. Apollo Hospitals provide doctors for the van and specialists for free consultations. Electronics Corporation of India, a governmental organization, supplies the satellite dish, while the Indian Space Research Organization (ISRO) handles placing the satellite in orbit. Active in social mobilization, micro finance and micro insurance, NGO partner Development of Human Action (DHAN) brings its knowledge of the target community to the project. To prepare for the pilot's launch in the first quarter of 2005, Philips customized a 'teleclinical' van complete with diagnostic equipment.

Learning gained during the pilot phase will be evaluated and we will refine the business model, including work on the delivery system and pricing. We also will seek partnerships with additional NGOs active in healthcare.

### Creating a new sales channel

The Philips Innovation Campus in Bangalore, India, launched a pilot project in June 2004 to sell Philips products in villages. They used the services of Self Help Groups (SHGs) to create a new sales channel. The SHG concept is popular in developing countries. In India SHGs manage and lend their accumulated savings and externally leveraged funds to their members. Self help groups cover more than 8 million families, with women representing 90% of the membership.

Collaborating with Myrada, an NGO that works to raise the living standards of rural populations around Bangalore using the SHG concept, Philips has been working with self help groups to sell wind-up radios. Considering that rural villages have power for only one or two hours a day, these radios offer a practical way to get news, music, crop prices and more.

The SHG quickly sold 200 radios to villagers at a cost of about EUR 13 payable in six monthly installments. The required upfront capital, funded by Philips and Innovation Center employees who 'adopted a radio,' was promptly repaid by the SHG.

We will launch a second scaled-up pilot during 2005 with a broadened scope, including more NGOs and regions in India, as well as a more extensive product range to meet the villagers' aspirations.

### IT Access for Everyone

At the 2004 meeting of the World Economic Forum in Davos, Switzerland, IT, industry and telecommunications leaders decided to start a project to develop innovative value propositions and business models to reduce the digital divide at the base of the economic pyramid. ITAFE was created – IT Access for Everyone – with



representatives from organizations including Accenture, AMD, Cisco Systems, Dell, the Institute for Connectivity in the Americas, Intel and Philips.

The ITAFE group has been focusing its research on understanding how to orchestrate both supply and demand drivers for a sustainable digital inclusion eco-system. They have chosen Brazil as a first pilot and will use the information gained for scaling to other Latin American, Asian and African countries.

The group has recommended continuing with phase two, focusing on priority employment, education and health services in a public-private partnership framework in urban and rural settings. While the initial aim may have been purely philanthropic, it was quickly realized that the most positive impact could only be achieved by developing a sustainable business model that supports the eco-system it operates in.



## Pioneering partnerships

M.P. Vasimalai, Executive Director of India's Development of Human Action Foundation, A. Bhaskaranarayana, Director of SatCom Programs and Program Director for the Indian Space Research Organisation, and K. Ramachandran, Philips India CEO, are firm believers in the importance of cooperation to bring project's like the DISHA (Distance Healthcare Advancement) pilot to life.

When he talks about the DISHA pilot, M.P. Vasimalai focuses on one word – cooperation. “This project is about being socially responsible in a new way,” says Vasimalai, the Executive Director of India's Development of Human Action (DHAN) Foundation. “We are bringing together the core competencies of several partners to build social capital in the community. It's a long-term approach and we will certainly learn a lot from the DISHA pilot.”

DHAN provides a vital link to the community, building trust and credibility for the project. “Our core competence is knowing how to operate in a way that works for the people we want to serve,” he says. “The community's perception of DISHA will be shaped by two things – transparency of cost and effective treatment.”

### Dealing with poverty

Vasimalai points out that a health emergency can quickly turn into a “calamity” forcing a family to take a loan of EUR 180 (or 10,000 rupees). “Typically these loans are with moneylenders at a high rate of interest, which means it can take some 10 years to get out of debt. Plus, people living in poverty pay more for lower quality services,” he explains. “Early intervention in a health crisis is critical in dealing with poverty. The right diagnosis can help reduce healthcare costs dramatically.”

A. Bhaskaranarayana, Director of SatCom Programs and Program Director for the Indian Space Research Organisation (ISRO), agrees.

“We have to bring quality healthcare to the people who would not otherwise receive it.”

ISRO works with NGOs to help bridge the digital divide, specifically in the areas of healthcare and education. “This is the first time we have partnered with a commercial organization like Philips,” Bhaskaranarayana notes. “For this to work, we must account for all expenses and develop a model that is self-sustaining.”

### Making healthcare affordable and available

Philips India CEO K. Ramachandran explains that to create that model, “We will use technology to reduce costs. Our goal is to bring affordable, accessible healthcare to the people in rural communities who need it.” In doing that Ramachandran and his team will bring simplicity to the consumer and keep the complexity at the back end.

“It's easy to think of a thousand reasons why something like this would not work. Bringing this type of project to life requires commitment and belief,” says Ramachandran. “We spent 2004 developing collaborative relationships and putting the foundation in place for our DISHA pilot. We've run workshops for our partners and will continue to nurture and develop those relationships. A project like this is only possible with strategic partnerships.”









# Social responsibility

We put people at the center. To design around people, you need to understand people. This means that all of our activities must be driven by insights into how customers and consumers experience the benefits of technology.

We create the kind of work environment that helps our employees around the world reach their full potential.

Through our social investments we are continuing our tradition of supporting the communities where we live and work.

# Our customers

At Philips we continuously explore new ways to offer innovative products and services to our customers and consumers.

## Our customers

The chart below provides an overview of our customers. Direct sales to consumers is very limited and relates primarily to sales through our employee stores. Most of our consumer products are sold through specialized or general retailers, with wholesalers as our primary customers in some cases. In terms of our professional products and services, we deal with end-users or wholesalers. In our OEM business, we sell components and subassemblies to other industries for use in their end products.

## Customer relationship management

Customer satisfaction is largely related to the experience with our products and services. To track that, we have a well-structured flow of customer feedback during the various stages of the lifecycle of our products.

To ensure dedicated follow-up on consumer complaints or requests for information, the Philips Global Consumer Service (GCS) organization (formerly known as PC3: Philips Customer Care Centre) provides after-sales consumer service, handles information requests and complaints, and carries out research on a global scale to measure the company's performance in these areas.

Additionally, our consumer divisions – Domestic Appliances and Personal Care (DAP) and Consumer Electronics – have procedures to ensure that action is taken on consumer requests, problems or complaints, leading to further product or service improvements. This includes root cause analysis where consumers have expressed an insufficient level of satisfaction. An example of this is the work done by Philips 'knowledge engineers' and marketing specialists.

## Customers influence our product creation process

Our product creation process includes a range of customer interactions. In addition to feedback on new product concepts and pre-testing of new products, we gather information on the unpacking and installing experience as well as product use, both shortly after purchase and in a later stage to monitor the product's reliability. This input is fed back into the product creation process for the next generation of products.

Methods used to gather data vary for business-to-business and business-to-consumer activities. Techniques used include contributions from advisory boards and focus groups, as well as feedback gathered by interviewing customers about product use in their own surroundings –

## Overview of main type of customer per product division

	consumers	specialized retailers	general retailers & multiples	wholesalers	small and large businesses	IT industry (PC + peripherals)	consumer electronics industry	telecommunications industry	building industry	governmental organizations	automotive industry	other industries	hospitals and clinics
Medical Systems		●	●	●						●			●
DAP	●	●	●	●									
Consumer Electronics	●	●	●	●		●							
Lighting	●	●	●	●	●				●	●	●	●	●
Semiconductors						●	●	●	●		●	●	
Other activities						●	●				●	●	

at home or in professional applications (shops, offices, hospitals, etc.).

Collaborating with Philips Design, Philips Lighting has conducted in-depth surveys with focus groups on social trends and behavior to discover unmet needs. This information is translated into potential lighting solutions for the different surroundings people live in. It's part of Lighting's commitment to live up to their mission, "to understand people to improve their lives with lighting."

### Meeting customer needs through partnerships

Strategic alliances have become an important part of business at Philips over recent years. They have many advantages. Alliances allow us to bring new products to the market that we wouldn't have been able to develop on our own. They increase the company's knowledge of different markets and industries, and they also give the brand a boost, as Philips is seen to be working with other highly regarded household names.

Over the past few years we have entered into a number of partnerships that have brought successful new products to the market. Recent alliances include Philips and Unilever joining forces to develop a new range of irons that will change the way consumers treat their clothes, and a global partnership with InBev to deliver the taste of draught beer in consumers' own homes with PerfectDraft. Other examples include an alliance with Nike to produce wearable audio equipment, a joint venture with Sara Lee/Douwe Egberts to market the Senseo coffee maker and a partnership with Nivea to develop a breakthrough in shaving.

Another example of direct customer involvement in innovation and product development is Lighting's Xenon automotive systems being developed in close cooperation with leading carmakers BMW and Toyota. Working with Toyota, we eliminated mercury from the lighting system for a more environmentally friendly automobile.

Philips Semiconductors management works with their leading customers to stay abreast of their strategic plans. With this close cooperation we align our Product Creation Process with our customer's strategy, which in turn is developed as a result of understanding end-user needs.

### Molecular imaging and diagnostics

Recognizing that patient-centric developments will drive advances in the area of molecular imaging and diagnostics, as well as integrated diagnosis and therapy, Philips Research is positioning its researchers in select academic centers of

medical excellence. With the support of the US National Institute of Health (NIH), they work alongside some of the world's leading clinicians.

Although sites will need to have an installed base of Philips imaging equipment, the research contracts will also allow the provision of additional Philips equipment and resources where justified. This joint research program, which is expected to see as many as 15 Philips Research staff working at clinical sites, is expected to deliver major results within three to five years.

### Privacy

Philips believes strongly in protecting the privacy of personally identifiable information. The Philips Privacy Policy is available on the web in 22 languages.

One of the current compliance problems facing international business is the transfer of personal data by multinational companies to their group companies located in countries without an adequate level of protection for personal data under the law. Philips plays a leading role in actively promoting the use of 'Binding Corporate Rules' as an alternative to effectively protect privacy in multinationals, while allowing maximum flexibility in the use of global systems.

As one of the first companies in the world to do so, Philips has drafted a Code of Conduct that creates a Safe Haven for personal data within Philips worldwide. The Code will be fully integrated in the Philips General Business Principles and a network of Privacy Officers will provide guidance for anyone who processes personal data within Philips. The Code will also provide for a complaint and redress procedure. The draft is currently in the final stages of discussion with the various Data Protection Authorities in Europe, as the Code requires government approval in the European Union.

As a leading technology provider, Philips seeks technical solutions to privacy issues. Philips Research developed a privacy solution for biometric template protection. This breakthrough technology allows for the use of biometric data as a secure and accurate identification method of individuals, while at the same time direct access to the biometric data itself is blocked for the owner/operator of the biometric identification scheme, thus protecting the privacy of the individual. Philips Research will continue to develop privacy solutions for various technologies, such as radio frequency identification (RFID), medical information systems and ambient home applications.

### RFID and privacy

Philips has shipped over one billion RFID chips, many of which are being used in contactless smart cards – an application that continued its rapid growth in 2004.

RFID technology enables the wireless transfer of digitally stored information on a carrier to a radio transceiver. Such a carrier usually takes the form of a label or payment card, which contains an IC (chip) and an antenna. Depending on the application, the transceiver (or reader) can be embedded in a dock-door in a distribution center, a payment terminal, or in the portals you find when entering and exiting a library or a store, for example.

Philips Semiconductors is a leading supplier of the chips that can be used in these labels and smart cards. Recently, Philips pioneered a new RFID-based technology called NFC, which allows for payment, ticketing and many other services to be implemented in the mobile phone.

RFID technology helps optimize supply chains (through use of 'radio barcodes' called the Electronic Product Code or EPC), keeps shelves full in the shops, enhances security in airline baggage handling and can help make passports and medication more difficult to counterfeit. Also, RFID can make secure payment more easy by bringing this and other services to contactless banking cards or even mobile phones. Creative use of RFID technology has the ability to touch and improve many aspects of our daily lives.

With RFID looking to rapidly gain momentum in the years ahead, industry participants need to clearly communicate how RFID technology is being used, and how it relates to average consumers. Concerns currently being voiced relate to the tracking and tracing of goods once taken out of stores by the people who bought them, as well as to unidentified and unauthorized access to, and use of, personal data stored on loyalty cards, passports or prescription medication.

In anticipation of applications of RFID in which consumers will be confronted with the technology, Philips has been and will continue to be very active in working with stakeholders to ensure aforementioned points are addressed. We are committed to help lead to an adoption of RFID which respects consumer's privacy rights, everywhere, always. Our approach is outlined in our RFID Privacy Position:

- Philips supports the RFID-resolution of the 25th Privacy and Data Protection Commissioners Conference, Sydney 2003, to provide consumers with notice and choice

- RFID labels should contain product data only
- Philips offers the world's (privacy) regulators help on understanding RFID and its implications on privacy
- Philips continues to find solutions for privacy and security issues with RFID
- Philips calls upon its customers and system integrators to install privacy-compliant systems and to respect consumer rights.

### Customer health and safety

Philips aims to supply high-quality products and services. Due to the wide variety of our products, each division issues a product safety handling procedure tailored to its business. To leverage best practices and develop a consistent One Philips approach, during 2003-2004 a cross-division working group with company legal and standardization experts explored product safety in depth.

The goal is to develop a Philips-wide product safety policy, while safeguarding the need for customized divisional implementation as necessary. The working group has created recommendations and developed a draft Philips Product Safety Policy. This is being evaluated by a cross-product division taskforce with the support Philips Intellectual Property and Standards (IP&S), and will be finalized and implemented in 2005.

Elements of the draft policy include:

- overall responsibility for customer health and safety assigned to Sustainability Board level
- a central product safety complaints procedure
- in depth training of all Product Creation Process teams on the intent of the policy, external regulatory requirements, and the tools and methods required to meet the policy requirements, and
- product labeling with details on how to contact Philips.

The policy also addresses regular assessments on compliance. Product recall and related procedures will remain a divisional responsibility in cooperation with relevant country management to ensure compliance with local regulation.

Attention to customer health and safety is an integral part of the Product Creation Process through focus on our EcoVision program's Green Focal Area hazardous substances (see page 60). Further, Consumer Electronics, DAP and Semiconductors have hazardous substance elimination initiatives including lead-free programs. While the divisions have different target dates to reach this goal, they are making progress.

# The benefits and risks of RFID applications

We asked Udo Helmbrecht about radio frequency identification (RFID) and privacy issues. Dr. Helmbrecht is President of the Federal Office for Information Security (BSI), the central IT security service provider for the German government.



## What are the benefits of RFID?

**UH:** There are many opportunities. One example is using RFID tags as public transport tickets.

If customers want to travel by train there is no need to buy a ticket. They simply enter the train with their RFID card, are identified by one of the readers at each door and the application 'knows' who is on board. At the destination the train application detects that the passenger left. Each month, customers get a bill with all relevant data – start and end of travel, train number, tariff, etc.

The benefit for carriers is also obvious as they are better able to measure the efficiency of their timetables. If there are only a few passengers on a train there is no need to have another train five minutes later.

## What is the connection between RFID development and privacy?

**UH:** RFID technology itself is not privacy related. However, RFID applications that include the user's personal information can be potentially risky.

## How?

**UH:** It's possible to intercept the communication between an RFID tag and a reader, for example. An eavesdropper could then see transmitted information that is not encrypted. Given an application with personal data – like loyalty cards with the owner's address and credit limit on it – privacy can be violated if an eavesdropper intercepts the data.

## What can be done to prevent this?

**UH:** There are numerous technical solutions, including deterring spoofing (or mimicking) of ID numbers by using mutual authentication

between tag and reader, encrypting transmitted data and hindering the tracking tags (and the related owner of a tag) by using random ID numbers.

But there is one big obstacle: Most of these security mechanisms are only available on expensive tags like dual interface smart cards. For mass-market application of RFID technology it is essential to have security features available on simple, inexpensive tags.

## How can industry resolve some of these issues?

**UH:** One main task of industry is to develop inexpensive RFID tags with security features like authentication and encryption. Further, with increasing distrust in RFID technology, it is important to publish the positive technical capabilities of modern RFID tags.

## What is the future of RFID?

**UH:** RFID will play a major role in eGovernment applications within the next five years. Machine-readable travel documents and numerous citizen cards will include contactless chips.

The future use of RFID will be based on international regulatory activities to include biometric data on travel documents and ID-cards.

## And privacy?

**UH:** Privacy concerns will grow with the increasing dissemination of the technology because data might be available 'anywhere anytime' and the owners might not be aware when their data is used. This challenge must be and will be met by strong security means.

The working group's recommendations take into consideration the revised General Product Safety Directive that must be implemented into EU Member States' laws, which covers all products supplied to consumers in Europe. Further, we recognize that the majority of our products are also covered by the Low Voltage Directive.

The Dutch consumer organization considers our approach toward health and safety "trend setting" given that it not

only covers customer health and safety, which is mainly based on dealing with environmental aspects of the product, but it also includes employee health and safety. Greenpeace also has commented favorably on our approach, even though they remain critical on the lack of clarity provided on the phasing out of PVCs.

# Our employees

Knowing that our continued success depends on our people around the world, we want to create an environment that reinforces teamwork, learning and inclusiveness – an environment that helps our employees reach their full potential.

## Working at Philips

As Philips continues to reinvent itself, the company is ever mindful of how transformation affects people.

There are significant ramifications of business changes like our moving toward a structure that is characterized by an increasing network of joint ventures, partnerships and alliances with third parties. Other shifts include moving production to developing markets.

Such change is not easy and requires a sharp focus on people to help manage the transformation process and ensure high performance. We strive to create an environment that fosters teamwork and collaboration, that motivates people and rewards them appropriately, and that respects the values and contributions of each unique individual, allowing them to feel truly included.

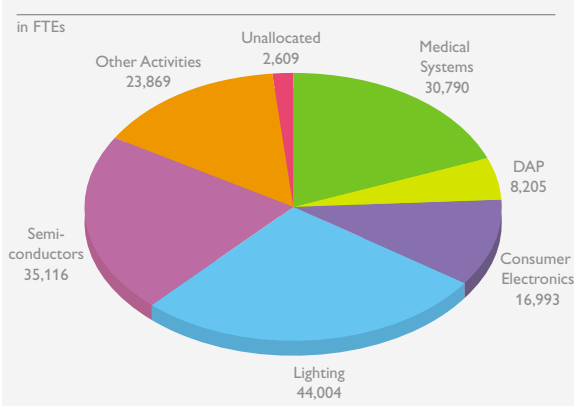
As the pace of change continues to accelerate, speed and innovation will be more and more important. That's why we encourage employees to be continuous learners, proactively managing their ongoing education and career development. To that end we are committed to fostering learning across units, regions, businesses and functions.

As One Philips, we believe in one set of values, known as 'The Philips Way – Our values in action.' Our values provide a solid foundation for all our actions.

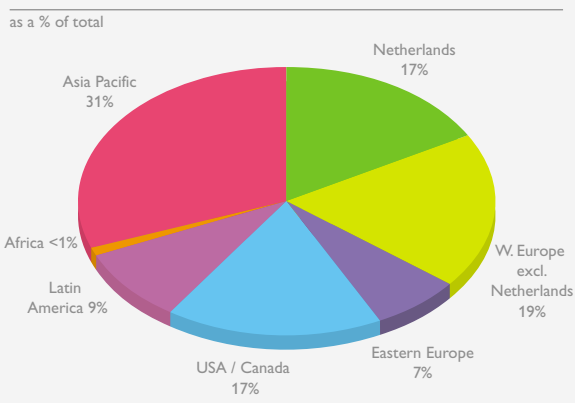
## Our employees

The number of Philips employees at year-end 2004 totaled 161,586. The following charts provide a breakdown of employees by product sector, geographic area, function, gender and regional origin.

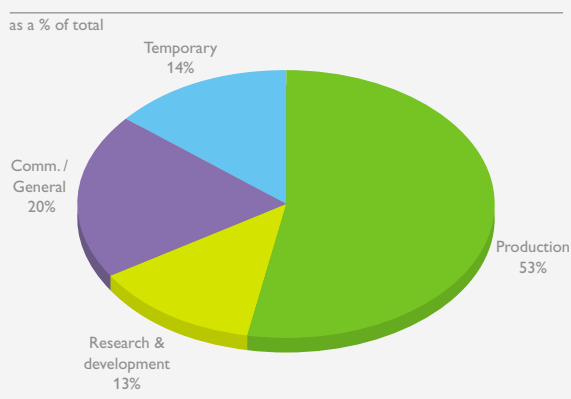
Employees per sector at year-end 2004



Employees by geographic area at year-end 2004



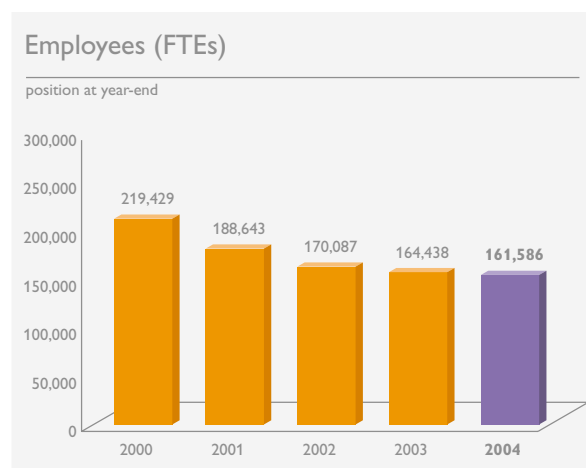
Employees by functional area at year-end 2004





### Changes in employment structure

The number of employees continues to decline, as a result of further divestments, additional outsourcing and continuing efficiency improvements.



The number of employees at the end of December 2004 totaled 161,586, a decline of 2,852 from December 31, 2003. Part of this reduction (418) is attributable to changes in the company's portfolio. The most important divestments were NAVTEQ (August 2004), involving a reduction of 1,546 employees and the divestment of the Consumer Electronics site in Kwidzyn, Poland, in December 2004, resulting in a reduction of 923 employees. On the other side, our total workforce increased by 2,374, with new consolidations. The most important were: the consolidation of the SSMC site in Singapore (Semiconductors), involving an increase of 1,047 employees, the acquisition of Neusoft (Medical Systems, China) adding 471, and Gemini (CE, USA) involving an increase of 584 employees.

Excluding these changes in the consolidated portfolio, the total number of employees decreased by 2,434, reflecting further outsourcing and the ongoing drive for efficiency. The sectors Consumer Electronics and Other Activities posted the most significant reductions, which were partly offset by a strong increase in Semiconductors.

### Employment changes in 2004 by sector

in FTEs	position end 2004	portfolio changes	real changes
Medical Systems	30,790	383	(206)
DAP	8,205	0	25
Consumer Electronics	16,993	(339)	(1,711)
Lighting	44,004	0	204
Semiconductors	35,116	1,047	894
Other Activities	23,869	(1,509)	(1,705)
Unallocated	2,609	0	65
Philips Group	161,586	(418)	(2,434)

The level of employment declined in all regions, with the exception of Asia Pacific, where the number of employees continued to rise.

### Employment changes in 2004 by geography

in FTEs	position end 2004	portfolio changes	real changes
Netherlands	26,772	(220)	(834)
W. Europe excl. Netherlands	30,425	(700)	(1,442)
Eastern Europe	12,045	(652)	(655)
USA/Canada	27,144	(334)	(750)
Latin America	14,084	0	(630)
Africa	411	0	2
Asia Pacific	50,705	1,488	1,875
Philips Group	161,586	(418)	(2,434)

The production area posted the strongest decrease in employees, reflecting the ongoing drive for efficiency improvements and outsourcing, particularly in more volatile markets. Excluding portfolio changes, the number of temporary employees rose slightly.

### Employment changes in 2004 by function

in FTEs	position end 2004	portfolio changes	real changes
Production	86,338	570	(2,250)
Research & development	20,378	(53)	(416)
Commercial / General	32,641	(404)	23
Temporary	22,229	(531)	209
Philips Group	161,586	(418)	(2,434)

## Creating a community coalition in Croydon

The decision to move Philips UK's headquarters out of Croydon could have added to the distress of this community that already had areas of significant deprivation. Instead, Philips spearheaded and largely financed a community-wide movement to establish a sustainable business group to serve Croydon long after the company would complete its September 2004 move to offices in Guilford and Redhill. Most of the 500 Philips employees who had worked in Croydon relocated to Guilford.

Philips left the community with a vibrant new organization – The Croydon Commitment – a consortium of local businesses, charitable organizations and civic groups working together to help Croydon survive and thrive. To establish this coalition, Philips worked with the Croydon Strategic Partnership (CSP), a local public-private voluntary-sector partnership, and then reached out to other community leaders. Business in the Community (BITC) came on board and assigned a staff member to the collaborative project, as did CSP and Philips, which covered at least 75% of the project team's staffing costs.

The project team met with representatives from local companies to tell them how they could help. The team suggested bringing in a business broker – a firm to encourage business involvement in local community issues. The business delegates agreed and the project team subsequently raised EUR 135,000 for the brokerage, with more than two-thirds coming from local businesses.

The Croydon Commitment includes:

- A forum where business can share best practice and learn about community involvement opportunities
- A commitment by Croydon companies to carry out at least three positive actions in Croydon each year – ideally across economic, social and environmental impact areas, and
- A business 'broker' to broker volunteering and other forms of community involvement from companies to local community organizations.

After nine months of work, The Croydon Commitment was handed over from Philips, BITC and Croydon Council to Croydon Business Broker Janine Jasper and a new management board. Their target is to recruit 30 companies and broker at least EUR 110,000 worth of volunteer time and in-kind donations. In the first six months, 23 companies signed on, and EUR 65,000 in cash and in-kind support has been contributed.

### Responsible transformation in Europe

Like other multinational organizations, Philips continues to undergo a transformation. The need to transfer some of the company's manufacturing activities is balanced by investments in what many call the knowledge economy. This impacts areas such as design, research activities and development work, and leads to the creation of new jobs and market opportunities outside Europe.

At Philips any decision about restructuring and possible job losses is never taken lightly and once such decisions are taken, the company will act responsibly, safeguarding the interests of our employees. This is clearly laid out in a position paper published in 2003 titled 'Responsible Transformation within Europe.'

We believe in addressing stakeholders, from employees and their representatives, to local politicians who represent their interests, to shareholders and opinion-leaders, including the media.

In this respect, Philips will continue to focus on improving employability. Professional development initiatives can empower employees by providing the resources and skills they need to develop further and/or find their next position.

### European Philips Forum

The European Philips Forum (EPF) was established in 1996 as a consultative platform in the region. This group meets with Philips management twice a year to discuss business developments of significant importance to employees of the Philips Group companies in the European Union, plus Switzerland and Norway. Representatives from Poland, Hungary and Czech Republic joined the EPF in July 2004, with the expansion of the European Union in May.

During the year a taskforce on Responsible Transformation was established. The objective of the group, which includes employees and management, was to review practices regarding transformation issues in Europe and further explore the issue of employability. To gather this information, the taskforce conducted two surveys.

The taskforce's analysis revealed that employees often preferred financial compensation to re-training/re-employment. They also discovered that the company position paper on 'Responsible Transformation within Europe' was mainly applied to restructuring in manufacturing.

Both management and employee representatives agreed that the transformation was carried out in a socially responsible manner in a number of cases, even though their views about the transformation process differed.

Regarding employability, it turns out that practices would benefit from a more consistent and inclusive approach. An example of a program for the lower-grade levels is the Philips Employment Scheme developed in the Netherlands. Establishing a structured training program for industrial operators in several sites can significantly improve employability. Comparable programs are being created.

The results of both surveys as well as the taskforce's recommendations will be used to improve our employability practices in the region.

### Employee engagement

Since 2002, we have been concentrating on employee engagement and its drivers, and monitoring our progress in this important area. While the more traditional concept of employee satisfaction is important, it is not as critical to organizational effectiveness as is engagement, a combination of attitudes and priorities that has a consistent and predictable impact on behavior.

Fully engaged employees tend to be more productive, conscientious and have higher levels of organizational commitment. In addition, research has shown that an engaged workforce tends to stay employed longer, miss work less often, have higher levels of customer satisfaction and service quality, attain and surpass organizational goals more regularly, require less training, be more productive and have comparatively lower workers compensation and accident claims.

We have broken with tradition after four global surveys (1994, 1996, 1999, 2001) and enabled our businesses to measure engagement at the time of their choosing, at least once every two years. We have established corporate standards and simplified workflows with standard processes and content on web-hosted applications. Employees answer a questionnaire consisting of 33 Philips core items and up to 17 business-specific items.

This surveying process, offers easy-to-use interfaces, on-demand availability and the capability to compare results across a number of dimensions. More importantly, this gives business leaders ownership for the process and results. Being close to the issues that drive engagement levels means that more attention is given to actions and



## Engaging employees to support growth

Philips China conducted an employee engagement survey in 2003. These results have been used to shape a long-term people strategy with a strong emphasis on the following five key areas:

- **Management behavior:** External consultants have worked with the top 50 Philips China leaders to prepare them for the challenges of growing the business in this important market and equip them with the tools to create an engaged workforce. This work will continue during 2005.
- **Talent management and career development:** TOTAL (Talent of Tomorrow Advanced Learning) focuses on high-potentials. Other career development initiatives include cross-product division projects and activities that provide high and top potentials with exposure to Philips executives.
- **Human Resources practices:** Programs include the formation of a China HR Council and a Policy Review Board (PRB). Comprised of HR leaders from the product divisions, the PRB reviews policies quarterly to ensure a One Philips approach.
- **New hire orientation:** China was one of the pilot sites to launch the global Philips In-Touch program for new hire orientation. Plus, November 2004 saw the launch of an extensive talent induction process with high potential new hires participating in this comprehensive 24-month program.
- **Informing and involving employees:** Initiatives include monthly information sessions led by senior management for all employees, as well as large town hall meetings and smaller product division or function specific town halls. Plans for 2005 include a new employee recognition program.

behaviors that can positively influence engagement and in turn, business performance.

We have created an Employee Engagement Index that allows us to report the level of employee engagement with a single figure, either as a % favorable or a mean score. The index is an average of three items – “Overall, I am extremely satisfied with Philips as a place to work,” “I would gladly refer a good friend or family member to Philips for employment,” and “I rarely think about looking for a new job outside of Philips.”

During 2004, a total of 102,793 employees were invited to participate in an employee survey. We exceeded our target of 75% participation, with 82,616 returned questionnaires, or an 80% response rate. The overall Employee Engagement Index for Philips is a 58% Favorable / 3.51 mean score, on a scale from 1 to 5. Since we have used a new set of items and a new answer scale, we are unable to compare 2004 scores with previous years. Future results will be compared with 2004 scores.

During 2005, we will conduct a first measurement for the businesses that did not survey employees in 2004, and conduct follow-up surveys in many of the businesses that measured in 2004.

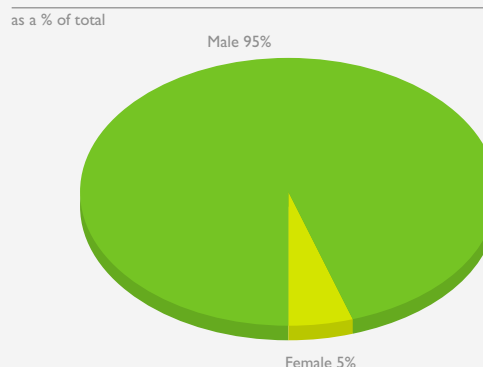
### Diversity and inclusion

In the company's Sustainability Report 2002, Philips announced that it wants to increase the percentage of women and non-Dutch nationals in key executive positions. The company is working to increase the number of women in senior management.

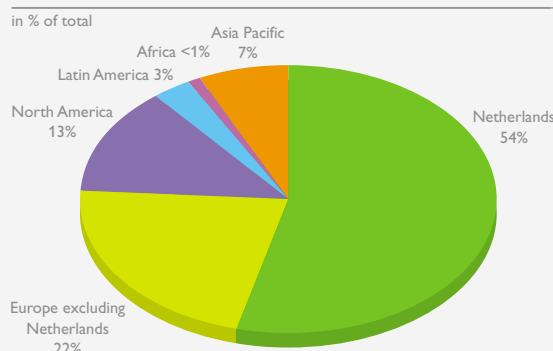
We want to raise the percentage to at least 10% within four to five years, more than doubling our 4% level in 2002. The percentage increased to 5% in 2003 and remained at 5% at year-end 2004. This is due mainly to the higher turnover of women executives. There were a total of seven terminations and one retirement during 2004, compared with two terminations in 2003. Hiring was also comparatively lower than in 2003, with a total of six versus two.

The number of leadership top potential female employees is more than 10%. This will help us achieve our target of raising the number of women in senior management.

Composition of Philips executives (total = 775) at year-end 2004

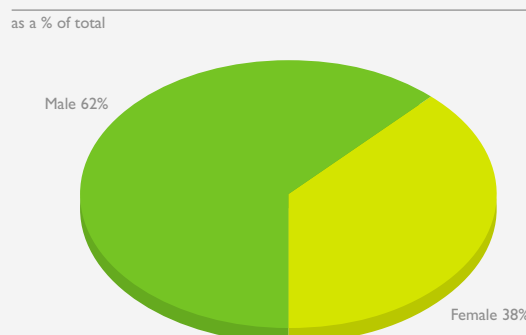


Regional origin of Philips executives at year-end 2004



Based upon a 92% response rate, figures from our Health and Safety Reporting system indicate that world-wide in Philips the percentage of females is approximately 38%.

Employees by gender at year-end 2004



This varies significantly by region and country. The percentage of female employees stands at a high of 50% in Asia and a low of 30% in the EMEA (Europe/Middle East/Africa) region, including 20% in the Netherlands.

Females represent 34% of total employees in North America, and 45% in Latin America.

#### Inclusion Index

To ensure a balance between making the numbers in terms of diversity and having the right culture to take advantage of the richness of our diversity, we have established an Inclusion Index that provides us a means to gauge where we stand and assess our progress.

The index is an average of the responses to four items from our employee engagement questionnaire used throughout the company – “I feel that I am part of a team,” “My ideas and opinions count,” “Philips values my contribution” and “Philips is committed to providing equal opportunities for all employees.” Our Inclusion Index received a 54% Favorable / 3.41 mean score, on a scale from 1 to 5, in 2004.

#### Progress in 2004

The year was dedicated to laying a solid foundation to support our global diversity and inclusion efforts. The Diversity and Inclusion Council, chaired by our President, reviewed progress at year's end and set the course for 2005 and beyond.

During 2004 we accomplished the objectives set forth in the Sustainability Report 2003:

- establishing the Philips Diversity and Inclusion Office and appointed a Vice President of Global Diversity and Inclusion
- launching the Global Women Executives Network and Champions Network
- creating the New Executive Hire's forum for feedback to improve and enhance the existing induction program to help new hires better integrate
- designating diversity and inclusion champions in each product division and region
- developing a clear process for measuring progress
- launching a mutual mentoring program to expose current top management to future company leaders coming from backgrounds unlike our traditional management group, and
- engaging top management and their HR business partners.

In the Sustainability Annual Report 2003 we said we would assess principal HR processes. We did not do so in 2004 because we made the decision to wait until we were further grounded in our diversity and inclusion initiatives. This will allow us to develop more effective guidelines for the assessment.

#### 2005 plans

In addition to maintaining the foundation laid in 2004, our 2005 plans include specific efforts to:

- increase diversity and inclusion leadership competencies at senior management level
- further raise awareness of diversity and inclusion at all levels of the company through established education and communication channels
- actively educate and engage the Human Resources function, and
- partner with the businesses and regions to embed programs such as affinity network groups and mutual mentoring throughout the company.

#### Learning and development

We believe that developing people is crucial to our success. To compete worldwide in a variety of different markets, we need individuals who can learn quickly, develop themselves and adapt to rapidly changing circumstances. That's why we introduced a One Philips approach to learning, starting with our Generic Core Curriculum, which includes learning programs in a number of areas – personal effectiveness, people management, working together and company awareness.

This global program gives many employees in Philips opportunities to grow and develop, getting the best learning experience wherever they are in the world. This broad range of consistent and carefully designed programs benefit people at all levels of the career ladder.

We launched 33 Generic Core Curriculum courses during 2004. Enrolment began with more than 1,000 participants in the first quarter and approached 5,000 by year-end. The target for 2005 is to double the number of participants.

Further, we developed global Functional Core Curricula in 2004 for Marketing, Sales & Key Account Management, IT, HR and Supply Management. The Supply Management Functional Core Curriculum was launched in 2004, and the others will be launched in 2005.

To deploy our global learning programs in both the functional and behavioral areas, Philips has established three regional learning centers – in North America, Europe/ Middle East/Africa (EMEA) and in Asia Pacific – that can reach a large number of employees in these regions.

We measure our employee perception related to training and development through the two following questions in the Philips Employee Engagement Survey: “I have the



## Diversity and inclusion at Philips

With the ground work set for driving diversity and inclusion, Tjerk Hoogheijstra, member of the Group Management Committee responsible for Human Resources Management, and Beckie Chan, Vice President of Global Diversity and Inclusion, talk about what that means to the company.

### How is diversity defined at Philips?

**TH:** Diversity is the existence of many unique individuals in the workplace, marketplace and community. This includes men and women from different nations, cultures, ethnic groups, generations, backgrounds, skills, abilities and all the other unique differences that make each of us who we are. It's about the things we see as well as all those things below the surface, like what's below the tip of an iceberg.

**BC:** A diverse workforce that mirrors our global customer base can help us better understand our customers and identify their needs. This can help us achieve our goal to create potential new markets that contribute to the bottom line.

### And inclusion?

**TH:** Inclusion occurs in a work environment where everyone has an opportunity to fully participate in creating business success and where each person is valued for his or her distinctive talents, skills, experiences, perspectives, etc.

**BC:** In an inclusive environment people are engaged. This enhances decision-making, and increases creativity, which in turn will help us live our vision and support our brand positioning.

### What does this mean for the company's leaders?

**TH:** Diversity and inclusion is an important dimension under our leadership umbrella. Inclusive leaders champion diverse views and foster a climate of transparency and dialogue where people feel safe to openly challenge one another. Such an atmosphere stimulates learning and innovation, and can help drive change.

**BC:** We are embedding diversity and inclusion in our existing HR processes, including our core curriculum, management development process and succession planning. And we work across our businesses and regions to make sure we have a holistic, One Philips approach.

### What kind of progress are we making?

**TH:** We have worked hard to build a firm foundation for diversity and inclusion. I'm very glad that Beckie has taken up this important challenge and is managing our initiatives on a global level.

**BC:** We believe we have the right focus and are working in a way that will get us to where we want to be. By doing the right things right – building awareness, embedding diversity and inclusion into the management development and other key HR processes, encouraging open dialogue and all the other things we talked about here – we are confident we will make good progress.

training I need to do my job effectively" and "Philips provides me with opportunities to learn and grow." Philips currently performs on average with other companies in our external benchmark group of companies that work with Kenexa, the company that handled our employee survey.

Some learning, of course, cannot be standardized, namely courses related to specific businesses and locations. These will continue to be organized by local HR to accelerate employees' readiness to achieve business objectives and contribute to organizational change.

### Health and safety

Philips aims to maintain work environments that are

free from all risks and hazards to the safety and health of employees, as well as contractors and others on company premises.

In 2004 we reviewed our policy on occupational health and safety, through a bottom-up approach involving Philips employees working in the area of health and safety in 23 countries in all regions. Their input was used to draft the policy. Approved at the end of 2004, the policy sets out our philosophy of zero tolerance for work-related incidents and disorders, and maintains the company's commitment to high standards at work (see page 92).





## Learning in context

Princess Máxima of the Netherlands (far right) presented schooling contracts to Najat Chenan (far left) and Tanja Jovanovic, participants in the Philips Employment Scheme, at an event marking International Women's Day on March 8, 2004. The Princess is a member of the Committee for the Participation of Women from Ethnic Minority Groups, which organized the event.

In the Netherlands, unemployment among ethnic minorities and migrants is nearly three times as high as among the native population. To promote inclusion and integration, a significant issue in European society given the recent wave of immigration, education and training is vital.

The Philips Employment Scheme, which was established in 1983, provides a combination of theoretical and practical training to the (long term) unemployed in the Netherlands. This program has proven effective for people with language or cultural limitations. After earning their industry recognized diploma for process operators, many successful participants have found job opportunities.

In 2004, we took this program further. Philips Netherlands, in cooperation with the Institute for Interethnic Management, the Dutch national institute for vocational training and education in the process technology sector, and the University of Tilburg, developed three additional modules for the Employment Scheme, focusing on multi-cultural issues.

Further, all production personnel working for Philips in the Netherlands will be offered the opportunity to train for an officially recognized vocational diploma to increase their employability. This project, started in 2004 in agreement with the Dutch trade unions, will be offered in 2005.

### Sharing our experience

This approach has been well received within the EU, where Philips has shared this knowledge with partners in Finland, Denmark, Belgium and Italy, as part of the EQUAL project – an EU initiative to promote a more inclusive work life through fighting discrimination and exclusion based on sex, racial or ethnic origin, religion or belief, disability, age or sexual orientation.

In November 2004, Philips has shared its experience in minority education programs at a conference attended by EU ministers responsible for integration issues in the 25 member states, Romania, Bulgaria, Croatia, Turkey, Iceland and Norway.

### Health and safety performance

In 2004 we made significant progress in implementing our program for standardized data collection and reporting of health and safety data throughout the company. As part of our ongoing efforts to improve the quality of data, we conducted training, as well as internal and external audits at various facilities around the world.

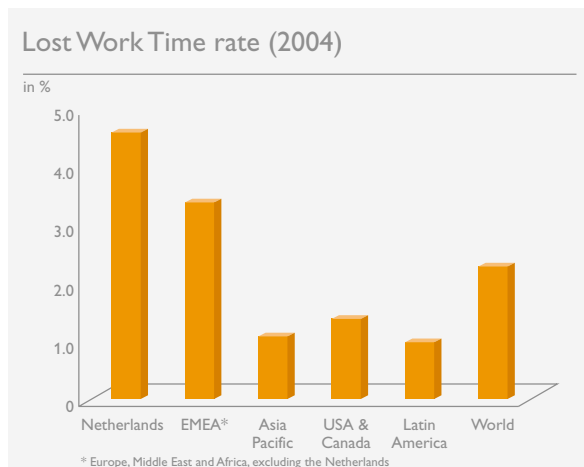
We are pleased to provide first results for two important parameters: lost work time rate and lost workday injuries.

On average during 2004, the reported data covered approximately 92% of all Philips employees in terms of

FTEs (full time equivalents). In 2005, the system will be further improved to fully achieve our standards of reliability.

According to the first results, we recorded in the year 2004 an average lost work time rate (absence from work with reported sick leave as a percentage of hours that could be worked contractually) of approximately 2.4% worldwide. However, levels of presenteeism differ per region because they are largely dependent on cultural factors, as well as different applicable legal and contractual compensation systems.

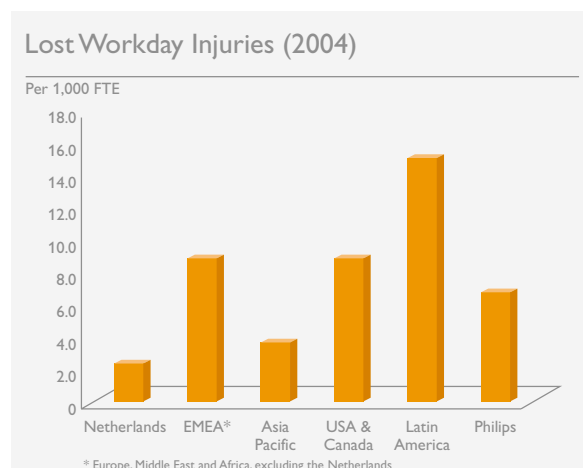
According to an initial assessment, on average approximately 6% of lost work time was reported as work-related (due to occupational injuries or illnesses).



\* Europe, Middle East and Africa, excluding the Netherlands

Interpretation of the standard definitions needs further improvement. Over time, we expect the reliability of these data to improve.

In 2004 we recorded 1,070 occupational injury cases causing the injured employee to be unable to work on the day after the injury (lost workday injuries). Regional differences in our safety performance, as illustrated below, appear to be less related to cultural or legal differences than to differences in industrial activities and labor and safety conditions. We are investigating the causes of these reported injuries and will develop an improvement program.



## Philips South Africa HIV/AIDS policy and practices

All 174 employees of Philips South Africa are insured for medical costs, either through the Philips Medical Aid Scheme or through their spouse's medical insurance.

Employees with HIV/AIDS are not treated any differently than other employees and therefore qualify for treatment and benefits. Employees can also make use of the Employee Wellness Program for counseling and information on lifestyle improvements to deal with HIV/AIDS. The Employee Wellness Program offers formal counseling by qualified psychologists, with the first two sessions provided at no cost and follow-up consultations charged to the employee's medical insurance.

Safety/First Aid officers and key staff have been trained on first level HIV/AIDS counseling and

are trained to deal with incidents. Philips South Africa also dispenses condoms free of charge to all personnel. In the event that individuals cannot perform their job as a result of AIDS-related illnesses or confirmed HIV status, the company will, where practical, modify and/or reassign the person's job function or place the employee on a disability pension, as reflected in the policy. While on disability, the employee will continue to have access to Medical Aid Benefits.

Through Employment Equity workshops, employees have been made aware of the HIV/AIDS program within the organization, as well as the legislative requirements regarding related issues such as discrimination and employment screening.

Philips South Africa supports South African Government initiatives like the annual National AIDS, by participating in the awareness campaign, which includes informational banners and mini first aid kits for employees.

In the framework of social investment, we support Cotlands, a South African sanctuary for orphaned AIDS babies. We have also collaborated with Love Life, an organization that deals extensively with AIDS issues in South Africa, which assisted us during our SOAR project (Supply Opportunities and Achieve Results) to raise awareness among students. The SOAR project is a major educational initiative to refurbish five schools in the Johannesburg area. Information regarding these and other projects are provided to staff via the Employee Wellness website.

The most serious accident reported in 2004 involved a bus collision in Manaus, Brazil, in January. Forty-five employees were injured and temporarily unable to work, accounting for approximately 20% of the total cases reported in Latin America for the year. Accidents related to employees' commutation are in principle excluded from Philips corporate health and safety reporting. However, injuries occurring during transportation arranged and managed by Philips, as was the case in Manaus, are considered occupational according to the applied definitions and therefore included in the database.

Our health and safety reporting system does not include reported fatalities in 2004. It is highly unlikely that any work-related fatalities occurred among Philips employees during the year.

#### Health and safety management systems

In 2004 the HR Process Survey Tool was revised and the rollout process was started. The tool includes a specific measurement of the maturity level regarding occupational health and safety management. Business units have started to implement this tool and in 2005 they will begin self-assessments, which will be followed later by peer assessments. This will help our organizational entities execute a gap analysis on the quality of their management systems and define improvement plans.

Philips Semiconductors has decided to have all of its major industrial sites comply with OHSAS 18001. Three sites already have been certified.

#### Human rights

As discussed earlier in this report, 2004 saw the worldwide rollout of the new version of the Philips General Business Principles (GBP). One of the material changes is a reference to human rights with due regard for the Declaration of Human Rights, including a number of clauses dealing with child labor, forced labor, right of association/collective bargaining, non-discrimination and equal pay, as well as payment and working hours, in reference to the International Labour Organization (ILO) Core Conventions.

To drive the practical deployment of the GBP, a set of Directives have been published, one of them being the 'Policy Statements on Conventions of the ILO.'

In November 2004 we established a taskforce comprised of members of the HR community across the company, involving the regions, product divisions and relevant corporate HR functions. Their assignment is to improve

## Stress policy works for employees

The costs of stress are significant. A significant cause of disease, job dissatisfaction and reduced productivity, stress leads to decreased efficiency and creativity, as well as increased mistakes. Other consequences include absenteeism and turnover.

Philips Leuven in Belgium has developed a program "to offer psychological and social preventive and curative interventions and therefore optimize well being in a professional working environment." To bring this mission to life, Philips works in close cooperation with the ISW (Institute Stress at Work), which collaborates with the KUL (Catholic University of Leuven).

Preventive measures include a three-day course for managers in supportive leadership, and employees are made aware of the causes and symptoms of stress. In terms of care, the Medical Department provides first-line support to employees with stress and other work-related problems. The program also includes 10-15 individual counseling sessions, provided by ISW and paid for by Philips, to help employees deal with job-related stress.

Employees appreciate the program and occupational stress cases have been reduced to nearly zero, with no cases of absenteeism related to mental stress.

the monitoring on our key social policies. Implementation of an improved approach to social performance and reporting is planned for mid-2005. Additionally the taskforce is to review existing policies to identify areas that need to be further strengthened or are missing, given trends and developments in society that require such.

# Social investments

Using a targeted approach to social investment, we link initiatives with the company's scope of business, focusing on health and education, preferably with employee volunteerism. Projects are selected based on their potential to improve people's lives by providing access to healthcare and education, particularly for the underprivileged.

In 2004 we formalized this in our Philips Social Investment Policy, shown on page 93. We also conducted an inventory of social investments at the local level, gathering information about 200 projects from 47 countries in all four regions. Approximately 75% of the projects fell within our two areas of focus.

## Our social investments

In 2004 we invested EUR 9 million in projects in our regions. The following pages highlight examples of our social investments in each region. Additional significant projects from around the world are listed on page 94.

### Europe Middle East Africa

#### Mobilizing after a terror attack

Philips employees moved quickly to help wounded children after the hostage-taking attack on the school in the Russian town of Beslan. They carefully assessed the situation to determine the best way to help.

In addition to the regional social investment budget set aside for such emergencies, employees from Medical Systems, Lighting and Semiconductors in Russia donated funds to purchase Philips Intensive Care Units for children's hospitals in Beslan, Vladikavkaz, Rostov-on-Don and Speransky Children's Hospital in Moscow. In addition, Consumer Electronics provided TVs for game rooms and the lobby at Speransky Hospital.

Employee volunteers installed the ICU equipment, repaired monitors and delivered the TVs.

#### Seeing education in a new light

Philips employees in Central Europe wanted to improve poor lighting conditions for children in underprivileged region schools. Using their lighting expertise and our products, about 30 employees 'relamped' schools in the Czech Republic, Hungary, Poland and Slovakia, installing 118,000 TLD 80 low-mercury lamps.

Employee volunteers conducted lighting equipment assessments, provided recommendations to the schools and did the actual work to replace the old lighting equipment. After each facility was relamped, the old lamps were recycled.

Thanks to this initiative, nearly 98,000 children are learning in 3,600 classrooms that meet European Union standards. Launched in 2002, this project will continue in 2005.

Thanks to Philips employees, nearly 98,000 children are learning in properly lit classrooms in the Czech Republic, Hungary, Poland and Slovakia. Some 30 volunteers provided their lighting expertise to evaluate and 'relamp' 3,600 classrooms.



YES participants Brianne Consentino (left) and Nalyn Yim work on a science project with long-time volunteer John Snyder, Business Systems Analyst at Philips Medical Systems in Andover, Massachusetts, US. To get children excited about science and technology at an early age, YES assignments include building such things as electronic circuit games or balloon-powered cars.



## North America

### Saying YES to science

Philips Medical Systems in Andover, Massachusetts, US, has long supported the Youth Explorations in Science (YES) program. YES gives students (grades 3-6) an opportunity to learn through hands-on life, physical and earth science experiments led by adult or young adult volunteers. In 2004 the North America region provided funding to expand the program to 20 after-school programs in the city of Boston's neediest neighborhoods.

YES stimulates children's enthusiasm for science and technology, while promoting scientific investigation and a sense of wonder in the world around them.

The basic formula consists of a small club setting in which four children and one adult or young adult (such as a high school or college student) are engaged in a hands-on science experiment or project. Children take their projects home after each session, where they may repeat the experiments or explain their scientific creations to family and friends.

Projects might include building electronic circuit games, balloon-powered cars or terrariums. Students might solve crimes using paper chromatography or experiment with flotation and density. They might explore light and reflection as they build periscopes or explore sound as they build 'thumb pianos.'

Volunteers are given a kit that contains detailed instructions, diagrams and materials to build or complete an experiment during weekly or biweekly sessions. Instructions include questions that volunteers may use to stimulate inquiry and some answers that provide selected scientific content. The leader does not have to be a scientist or technician. Experiments and instructions are designed for the "layperson," thus not limiting volunteer participation.

Plus, the program can bring science education to students in non-traditional settings, such as hospital pediatric wards, boys and girls clubs, and community centers — at no cost to parents, teachers or the host organizations.

YES encourages teamwork and provides children with a sense of belonging in an environment that promotes creativity and develops self-esteem, while helping children develop cooperative learning skills through group interaction. Students are confident to work and learn at their own pace and they take pride in completing their projects.



Students between the ages of 7 and 10 years old enjoy 'Learning with Nature,' a program that serves public school students in São Paulo, Manaus, Varginha, Recife and Mauá, Brazil. The program promotes special activities developed by Philips employees who volunteer to work on the project.



## Latin America

### Raising students' awareness

Philips Brazil is known for its community involvement. Two of the company's projects focus on raising awareness about two important global issues – the environment and HIV/AIDS. Activities include teaching young people about the environment through the 'Learning with Nature' program, and about HIV/AIDS and teen pregnancy with the 'Donate Life' project.

In total some 700 Philips employees volunteer their time on these ongoing projects. We have included these initiatives in previous reports and are pleased to provide an update.

### Learning with Nature

Designed to awaken environmental consciousness in students between the ages of 7 and 10 years old, 'Learning with Nature' serves public school students in São Paulo, Manaus, Varginha, Recife and Mauá. The program promotes special activities developed by Philips employees who volunteer to work on the project. The objective is to awaken the children's natural curiosity and teach them to appreciate and to preserve the environment.

The project began in 2002 with a focus on environment and education. As the project evolved, we chose to focus on biodiversity and its importance in maintaining life on the planet.

In total, the project reaches 24,000 students from 1<sup>st</sup> to 4<sup>th</sup> grades, and involves 578 teachers and 112 schools in the states of Amazonas, Pernambuco, Minas Gerais and the São Paulo metropolitan area, in addition to local environmental organizations and Philips volunteers. The project has been recognized by UNESCO and the Brazilian Ministry of Education.

Brazilian high school students are better informed about HIV/AIDS, other sexually transmitted diseases and teenage pregnancy thanks to Philips employees who participate in the company's 'Doe Vida' program. Translated 'Donate Life,' this project has reached more than 69,000 students.

Philips volunteers have attended an eight-hour training program covering medical systems, statistics and the emotional impact of HIV/AIDS, including dealing with prejudice. These employees share this learning with students and teachers. A Philips medical doctor provides information on human anatomy, sexually transmitted diseases, pregnancy and condom use, while a company attorney discusses legal issues.

Voluntary health workers weigh a baby and update records in Bishnupur near Kolkata, India. Philips has adopted 15 villages covering 300 women and their infant children through a partnership with the Child in Need Institute. With a strong focus on proper nutrition, one of the goals of this program is to stem the rate of infant mortality.



## Asia Pacific

### Empowering those less privileged

Philips India supports programs that promote basic health and education to the less privileged. The company's Community Involvement Teams work with established social service organizations to make a difference in people's lives.

Through a partnership with the Child in Need Institute (CINI), Philips has adopted 15 villages covering 300 women and their infant children. CINI has worked for more than 30 years to guide and educate women and children near the city of Kolkata, formerly Calcutta. Voluntary health workers trained by CINI visit door-to-door to identify women in need, particularly pregnant and lactating mothers. One of the goals of this program is to address malnourishment to stem the rate of infant mortality in these villages.

Working with Trust for Reaching the Unreached, Philips reaches out to 15 villages and nearly 25,000 people near Vadodara in Gujarat. Life in these villages is in the hands of the women, so their health and welfare determines the villages' wellbeing. Young children's health is also monitored regularly and voluntary health workers visit schools to educate children on hygiene and disease prevention.

### Educating rural youth

Through a company initiative named Samvardhan, Philips has 'adopted' 110 young boys and girls in the hill station of Lonavla. The modern Mumbai-Pune expressway passes through Lonavla, bringing the challenges of development to these children from traditionally agricultural families. Facilitated by the social agency CASP – Community Aid and Sponsorship Program – Philips provides technical knowledge, social skills and classes in spoken English to prepare these children for better employment opportunities. Philips engineers conduct advanced training in electronics. Other subjects include public speaking taught by industry professionals.







# Environmental responsibility

With a tradition of sound environmental policy for more than 30 years, we are guided by the basic principle that prevention is better than cure.

We regard environmental improvement as an opportunity for innovation, and we work to minimize the impacts of products, processes and services. To meet this challenge, we began establishing a series of four-year action programs more than a decade ago.



### The world around us

Earlier in this report we discussed the key challenges facing the world. In terms of the environment, we believe the current significant issues for our company – and our industry sector as a whole – relate to global warming, chemical content of products and take-back and recycling. In the following pages, you will read about how we are dealing with these concerns.

### Global warming

The Kyoto accord took effect on February 16, 2005, imposing limits on emissions of carbon dioxide (CO<sub>2</sub>) and other gases scientists attribute to climate change – rising world temperatures, melting glaciers and rising oceans. The agreement targets CO<sub>2</sub> and five other gases that can trap heat in the atmosphere and are believed to cause global warming. A total of 141 nations, including the European Union have ratified, accepted, approved or assented to the pact, according to United Nations data.

Our activities contribute to CO<sub>2</sub> emissions both directly and indirectly. The use of fossil fuels, such as natural gas, oil or coal, and emissions of chemical substances like Per Fluorinated Compounds (PFCs) during production in our Semiconductors division activities, for example, contribute to global warming. Purchased electricity used in our facilities results in indirect CO<sub>2</sub> emissions from fossil fuel driven power plants.

We have made the reduction of energy consumption, and the resulting decrease in the emission of global warming

gases, a priority at Philips since the early 1980s. You will find results on page 66.

Consumers contribute to global warming by using electricity and electronic equipment. Reducing the power consumption of these products has been one of the main focal areas in our EcoDesign activities over the years. The aim is to offer consumers products with superior environmental performance, including minimal energy use in standby mode or lower energy consumption during use, compared to predecessor products or commercial competitors. This lowers the costs of use for the consumer and has a positive effect on global warming.

The upcoming Energy using Products Directive (EuP) will further strengthen these efforts. The aim of this initiative is to provide eco-design requirements for energy using products in the EU. Philips Lighting, for example, already offers energy-efficient lighting solutions. The challenge will be in solving the burden of higher investment costs to accelerate upgrading. Another example is at Philips Consumer Electronics where several energy-efficient LCD TV backlighting technologies have been introduced.

Our approach also includes providing consumers with advice on energy consumption in the directions for use that accompany these products. Examples of our top EcoDesigned products are highlighted on pages 62-65.

## Relative impact

Overview of CO <sub>2</sub> emissions Direct and indirect emissions	Worldwide	Netherlands	Europe*	USA/ Canada	Latin America	Asia Pacific	
Philips total CO <sub>2</sub> emissions	1,609	305	345	293	51	615	ktons
National/global CO <sub>2</sub> emissions**	24,101,830	177,880	5,846,270	6,184,160	1,209,760	7,421,910	ktons
Percentage of total	0.007%	0.172%	0.006%	0.005%	0.004%	0.008%	
Overview of energy consumption	Worldwide	Netherlands	Europe*	USA/ Canada	Latin America	Asia Pacific	
Philips total energy	28.4	5.9	7.3	4.7	1.2	9.3	PJ
National/global energy**	431,481	3,262	107,898	106,363	25,626	131,975	PJ
Percentage of total	0.007%	0.181%	0.007%	0.004%	0.005%	0.007%	

\* Excluding the Netherlands

\*\* 2002 data

(Source: International Energy Agency)



### Chemical content of products

Eliminating and minimizing use of hazardous substances in our products has been one of our priorities since the start of our environmental activities three decades ago, and is another important focal area in our EcoDesign activities. While we have long had a common system for managing chemical substances in production, lists for chemical content of products were not uniform and consistent throughout the company. Thanks to the work of a cross-product division task force, we established in 2004 a company-wide policy list with banned substances for our products. This list is also used in our approach toward suppliers.

A specific issue that has received increasing attention over the past years is lead-free products. Our divisions have implemented extensive programs and adapted their product specifications and processes to live up to our own standards as well as fulfill legislative requirements. Currently Philips has introduced several lead-free products.

### Take-back and recycling

In the mid-1990s Philips initiated, a project called 'Apparatour', aimed at developing a complete understanding of the recycling possibilities of the Waste of Electrical and Electronic Equipment (WEEE). In cooperation with the local authorities in Eindhoven, the Netherlands, and a substantial number of villages around the city, the project included investigating costs, logistics and the applicability of disassembly techniques. Disassembly was tested at the recycling company Mirec, a Philips subsidiary at that time. Today Mirec is part of the Australian-headquartered Sims

Group, a multinational company providing recycling solutions.

The learning gained during this project has been used over the years to support and help format upcoming legislation in Europe on take-back and recycling in a pragmatic way. One of the challenges was in determining how to deal with the costs of these activities, as they were not incorporated in the product price often sold more than a decade ago. Specifically, electronic and small electrical products contain only fractions of materials that have any value on the market for secondary raw materials. This was clearly out of balance with the substantial costs of logistics and labor cost for disassembly and recycling.

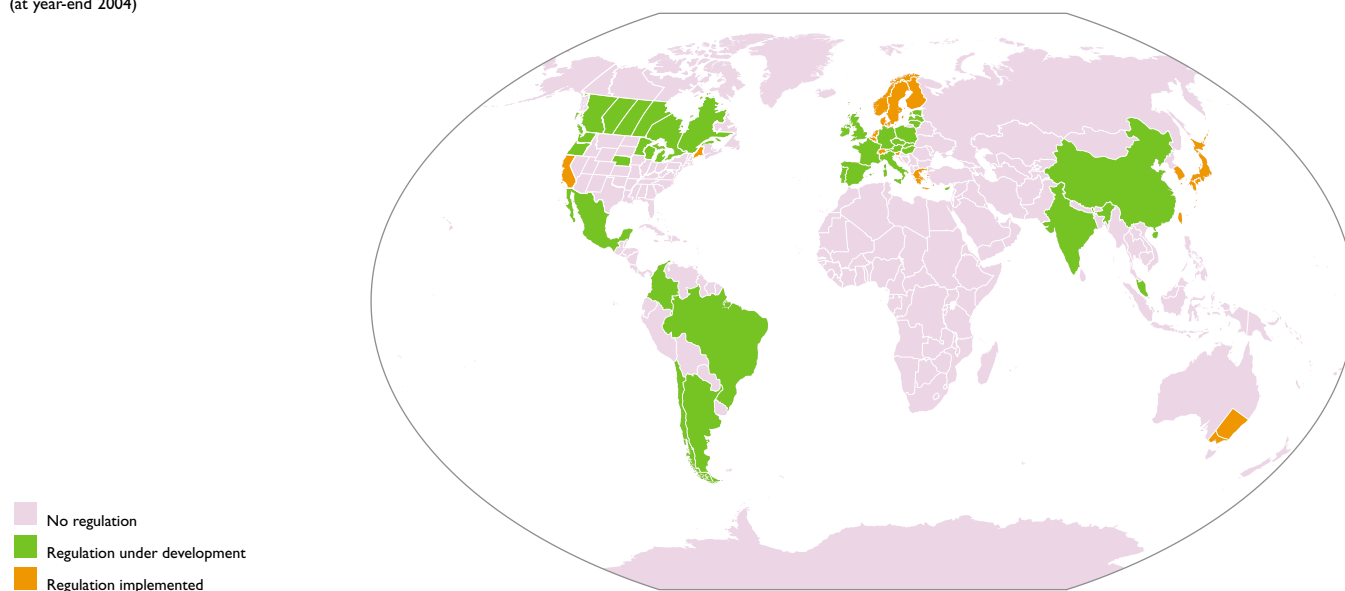
Another issue was the financing of products of older brands that had disappeared from the market, so called 'orphans'. The visible fee and organizing the cooperation between competitors and retail shops as well as municipal waste disposal stations as collection points for instance, has become one of the frequently applied solutions for these types of waste streams in different European countries.

One of the project's outcomes was the decision to cooperate with competitors and the concept of creating independent foundations to organize logistics and select certified recycling companies.

Legislation concerning the take-back and recycling of electrical and electronic equipment is also being shaped in countries like the US and China, among others.

## E-waste regulations

(at year-end 2004)



We work with competitors via our local organizations, taking an active stance to develop similar models.

### Products

Building on Philips' tradition of innovation and technological expertise, we have developed procedures for Environmentally Conscious Product Design – what we call EcoDesign – that deal with all phases of product development.

To support the EcoDesign process, Philips' EcoVision program requires focusing on the following five Green Focal Areas when developing products.



Weight



Hazardous substances



Energy consumption



Recycling and disposal



Packaging

These focal areas were introduced as part of our first EcoVision program in 1998. Over the years we have realized there is a need for customization to reflect areas of particular relevance for their businesses.

Energy efficiency for our Lighting division products is expressed in efficacy, which is the amount of visible light produced (lumen) per Watt (lm/W). For other products, energy consumption is expressed as kilowatt-hours per year (kWh/year), based on average annual use.

Packaging reduction and the resulting savings in transport and logistics is an area of particular concern for Consumer Electronics, driven by cost and environmental considerations. To deal with this challenge, Consumer Electronics is focusing on reducing packaging volume and adapting packaging dimensions to increase shipping efficiency by being able to load more in a container. This is in addition to work being done to reduce packaging weight.



## A perspective on take-back and recycling in the US

We talked to Mark Murray, Executive Director of Californians Against Waste (CAW), to get a view on the complexities of the take-back and recycling issue in the US. CAW is a non-profit grassroots organization that advocates policy initiatives at the local, state and federal levels.

"It's inevitable that we have a patchwork of legislation on take-back and recycling in the US," says Mark Murray, Executive Director of the Californians Against Waste. This is due to the fact that legislation is growing increasingly decentralized, with states "going their own route" in this area.

Murray believes calling for advanced disposal fees alone is overly simplistic. "We need to look to Europe where the legislation is comprehensive, dealing not only with take-back and recycling but with phasing out hazardous substances in the design phase," he explains. "Europe addressed the big picture problem by telling industry what the objectives were, asking business to come up with the solution and figure out how to implement it."

In the US, Murray sees a piecemeal system rather than the multi-state approach embraced by Europe. "Industry here is fighting each

other. If industry doesn't step forward, government will," he notes.

California's Electronic Waste Recycling Act went into effect on January 1, 2005. Retailers collect the Electronic Waste Recycling Fee on covered electronic devices from consumers. Key elements of the Act include:

- reduction in hazardous substances used in certain electronic products sold in California
- collection of an electronic waste recycling fee at the point of sale of certain products
- distribution of recovery and recycling payments to qualified entities covering the cost of electronic waste collection and recycling
- directive to establish environmentally preferred purchasing criteria for state agency purchases of certain electronic equipment.

"In general, the history of environmental policy has often been California taking the lead.

We may see other states pick this up," Murray says. "Maine's e-waste legislation is a shared responsibility solution. What we have are different legislative models on each coast – one embraced by one part of the industry and others. Some states will follow Maine, others California and others will come up with something in the middle."

Murray believes, "There will be a struggle until one approach shakes out. It's like the electronics industry itself. We have seen a variety of standards until one standard emerges."

The Green Flagship products shown on pages 62-65 provide details on packaging weight reduction. Information about the effects of the changes in volume and dimensions for Consumer Electronics products can be found on page 66.

Lifetime is a major quality indicator for our lighting products. Longer life reduces service costs of lighting gear and improves efficient use of material resources, as products last longer before they go into a recycling or disposal phase. In 2004 our Lighting division introduced lifetime as a new focal area, represented by the icon below.



Lifetime

### EcoDesign

To step up our efforts in EcoDesign, as part of EcoVision 2002-2005 we introduced the use of a maturity matrix that focuses on product creation process maturity to determine what we need to do to reach world-class status. The EcoDesign maturity matrix can be found on page 95.

In 2004 we decided to gather information on maturity further down in the organization – at the level of the autonomous development centers. During 2005 we will start collecting data at that organizational level for the first time.

### Green Flagships

Our top EcoDesigned products achieve Green Flagship status. This means that after having gone through divisional EcoDesign procedures, a product or product family has been investigated in three or more of the Green Focal Areas and proven to offer better environmental performance in two or more of those areas, compared with its predecessors or closest commercial competitors. When a product is compared with more than one competitor, the results are expressed as an improvement compared to the average of the competitors' performance in the investigated focal areas.

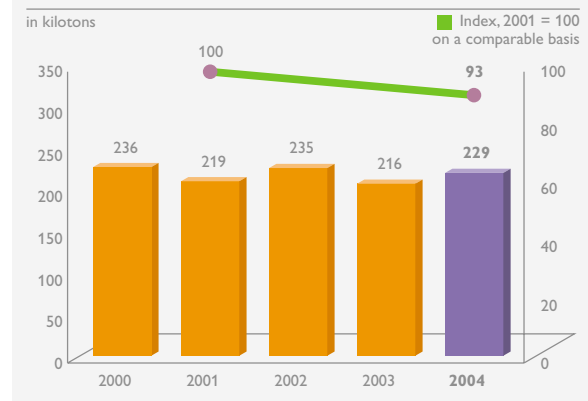
To continue to drive innovation and the development of environmentally responsible products, the current EcoVision program calls for one Green Flagship product per product division each year.

In 2004 four product divisions fulfilled their commitment to developing at least one Green Flagship per year and a total of 21 were put on the market, featured on the next following pages.

### Packaging

Wherever possible Philips' product packaging must be reusable or recyclable. According to the EcoVision requirements, the company must maintain packaging at 2001 levels, while the recommended target on a comparable basis is a 10% reduction for period 2002-2005.

#### Total packaging material

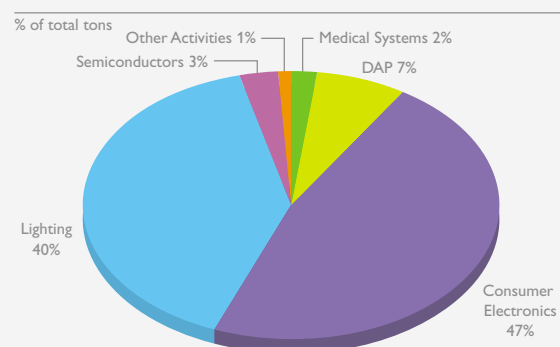


Philips packaging materials in 2004 amounted to 229 kilotons, an absolute increase of 6% from 2003. In comparable terms with respect to 2003, packaging materials increased by 4%.

This increase is mainly attributable to Consumer Electronics where packaging increased 7% on a comparable basis. This is due to increased use of packaging in the CE's Mainstream Displays business, resulting from a shift to larger screens and flat displays. Philips Lighting, accounting for 40% of the packaging total, remained at the same level as 2003.

The overall comparable decrease at company level based on the above data versus the base year 2001 is 7%.

#### Total packaging by sector in 2004



# Green Flagships



## Comprehensive surveillance

The M3176C USB 2-Channel Recorder is part of the IntelliVue Information Center, which combines the real-time monitoring surveillance of a central station with sophisticated clinical analysis tools. Compared with its predecessor, this recorder reduces weight 39%, includes 29% less packaging, reduces energy use 8% and improves recycling and disposal 12%.



## More with less

The 19.6-inch MML1921 monitor can be used in both landscape and portrait positions. It weighs 9% less than its smaller 18-inch predecessor, and by using one box for the monitor and pedestal – instead of the three boxes used previously – packaging is reduced by 35%.



## Medical Systems

Philips Medical Systems was an early adopter of EcoDesign. Using a modular approach the division is able to zoom in on a specific element to improve a product or system. Environmentally friendly design is particularly in keeping with the mission of Medical Systems' customers.

## Intelligent design

With its intelligent control and advanced ergonomic design, the iU22 ultrasound system delivers a range of high-performance features, including next generation, real-time 4D imaging, voice-activated control and annotation, and automated image optimization technologies. Compared with its predecessor, the iU22 weighs 22% less, eliminates 82% of the hazardous substance mercury, reduces energy 37%, uses 20% less packaging and offers a 30% improvement in total weight of recyclable material.





### Lower total cost of ownership

With its large screen and great performance, plus SmartManage for remote, LAN-based monitor management and low power consumption, the Philips 190S5 delivers convenience and an outstanding return on investment. This monitor reduces energy consumption 23% and uses 44% less packaging, compared with the average of its closest commercial competitors.



### On the move

Innovative products like the Xenium 9@9c are designed to make your life more simple – at home and on the move. This phone weighs 21% less and uses 62% less energy than its closest commercial competitors.



### Ready to wear, ready to go

This wearable MP3 player offers four hours of MP3 or eight hours of WMA music on the go. The KEY013 weighs 39% less, uses 87% less energy and reduces packaging 47%, compared with the average of its closest commercial competitors.



### Stylish and compact

The compact, ultra slim design of this DVD-Player fits everywhere and goes anywhere. The DVDP520 uses 51% less energy and 13% less packaging, compared with the average of its closest commercial competitors.



### Natural pictures, superb sounds

Pixel Plus technology delivers more vivid details while Virtual Dolby Surround offers a cinema-like experience. This 32PF9956 Flat TV uses 53% less energy and reduces packaging 25%, compared with the average of its closest commercial competitors.



### Consumer Electronics

Philips Consumer Electronics developed a framework to measure environmental performance of products. Thanks to a structured benchmarking process, designers are able to make comparisons between competitors and gain insights into industry trends. Armed with this information, they chart their roadmap to achieve best-in-class environmental improvements in next-generation products.

This disciplined approach combined with challenging targets – including a requirement that its products be 10% more energy efficient than competitor products – has led to strong results.

### Other Green Flagships introduced in 2004

- MCV250 CD Cassette Player
- 29PT7333 29-inch TV
- Key015 MP3 player





### Designed for consumers and the environment

The innovative Azur Precise has a unique Steam Tip designed to make ironing difficult-to-reach places much easier. Compared with the average of its closest competitors, the Azur Precise weighs 5% less and the environmental impact of packaging is 59% less.



### Domestic Appliances and Personal Care

Philips Domestic Appliances and Personal Care has long been on the forefront of making packaging out of recycled material. The division has made significant investments in this area and also focuses on reducing the weight of its products.

### Semiconductors

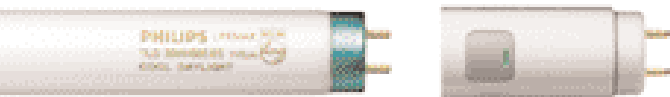
Philips Semiconductors has adopted a life cycle, holistic approach to minimize environmental and social impacts from raw materials, manufacturing, use and disposal. Semiconductors drives miniaturization and improved energy efficiency. Plus, our lead-free initiative calls for the removal of lead from our entire device portfolio, without adversely affecting technical specifications or our customers' manufacturing processes. With the majority of our products already qualifying as lead-free and meeting the latest legislative requirements, we expect to reach full conversion well before new legislation comes into effect. Along with other product information, Semiconductors' new Chemical Content Database gives customers all the information they need.



### Low power watch circuits

The PCA200X family of watch circuits has the lowest power consumption of any circuit on the market and is programmable to any modern watch motor. Launched in 2003, the PCA2002U/10 watch circuit weighs 95% less, is free of hazardous substances including lead, uses 46% less energy and 89% less packaging, compared with its predecessor.





### Easy cost savings

The innovative new Click-2-Save lighting system saves costs and energy in just two simple clicks. This system reduces the hazardous substance mercury by 63%, uses 18% less energy and offers 15% better lifetime, compared with its predecessor.



### Lighting

Environmental performance is increasingly important in our lamps business. Main drivers are the desire for lowering the total cost of ownership and increased awareness for environmentally superior products, combined with tighter legislation.

We have a full range of Green Flagship products that meet these needs and are beneficial both for our business and the environment. These products are more energy efficient, lifetime reliable, smaller and contain less hazardous substances.



### Electronics in urban lighting

CosmoPolis is a new generation of lamps and gear systems, bringing innovation to outdoor lighting. CosmoPolis Gold 6600 lumen weighs 37% less, eliminates the hazardous substance lead and uses 29% less energy than its predecessor.



### Maximum energy savings

ALTO Energy Advantage 25 watt T8 fluorescent lamps are the lowest energy consuming 4-foot T8 lamp on the market. This lamp reduces the hazardous substance mercury by 40%, uses 11% less energy and improves lifetime 30%, compared with the average of its predecessor and a commercial competitor.



### Designing with light

The MASTER Colour Elite TC 35W is an excellent choice for display and accent lighting. This lamp contains 14% less of the hazardous substance mercury, reduces energy 56% and offers 129% better lifetime, compared with the average of its closest commercial competitors.



### Masterful performance

Philips MASTER TL-D Xtreme offers businesses optimum lighting performance, with less early failures and a longer lifetime thanks to our innovative X-technology. This product uses 54% less of the hazardous substance mercury, reduces packaging 22% and improves lifetime 33%, compared with the average of two commercial competitors.



### Other Green Flagships introduced in 2004

- CosmoPolis White
- Master QL 85 watt
- Master TL-D Xtra



# Packaging and transportation

During the Product Creation Process at Philips Consumer Electronics, designers at the Global Development Centers scrutinize packaging and look for ways to achieve volume reductions.

We benchmarked our packaging with the best in class in the industry, and discovered that our requirements were too stringent. In other words, our products were “over packaged.” We carried out extensive testing of new, smaller packaging, tracking it from factories in Asia to retail outlets in the US and Europe, discovering that it provided more than adequate protection.

## Reduced packaging volume

This redesign of our packaging focuses on the reduction of packaging weight, combined with a change of dimensions and volume reduction. These changes enable us to load more products in a container, reducing costs and benefiting the environment. In addition to the packaging weight reductions mentioned on page 63, the resulting increase of number of products per container for these Green Flagships are the following:

KEY013	120%
190S5 LCD monitor	95%
32PF9965 Flat TV	55%
DVD-Player DVDP520	52%

We have defined opportunities that will enable us to reduce the cost of forwarding and distribution substantially by the end of 2005.

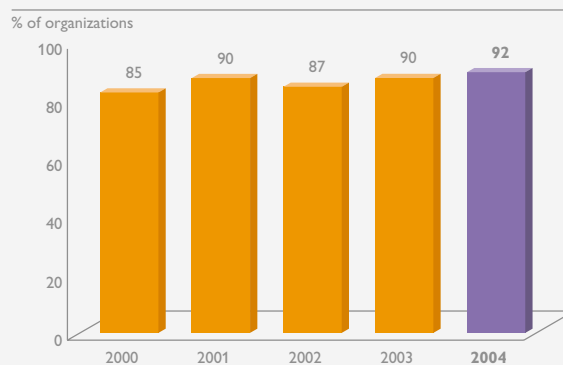
## Production

Philips strives to make effective use of resources and has set targets to optimize its processes. The aim is to reduce environmental impacts, achieving cost savings and improving efficiency.

## ISO implementation and certification

Company policy requires that all manufacturing sites achieve ISO 14001 certification and introduce environmental management systems to realize this goal.

Percentage of reporting organizations  
ISO 14001 certified



The percentage of certified units at year-end 2004 rose to 92%. The result includes 12 newly certified reporting organizations, 12 certified reporting organizations that were divested and four whose certificates expired.

## Energy

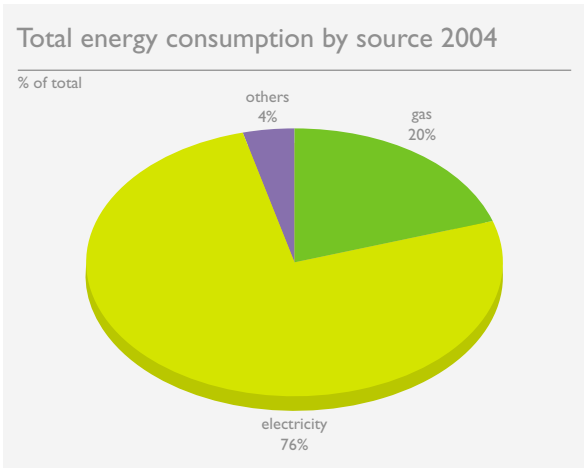
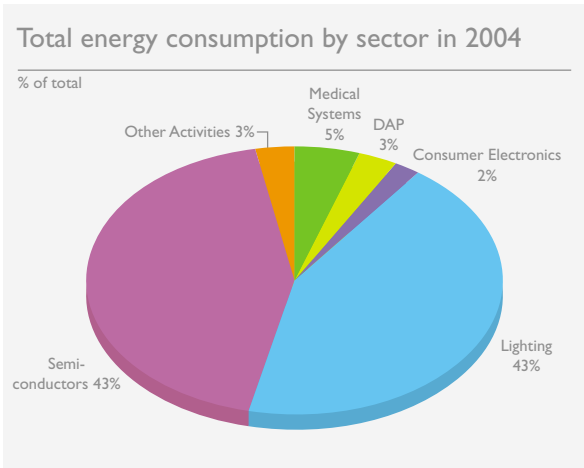
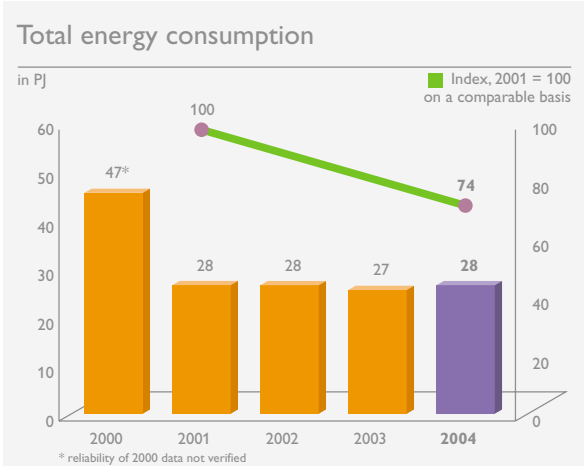
Philips measures energy use and applies efficiency measures worldwide. Because energy generated by burning fossil fuels causes the emission of CO<sub>2</sub>, a greenhouse gas that contributes to global warming, and energy reduction can generate cost savings, EcoVision 2002-2005 calls for a 10% reduction in energy use.

Absolute energy consumption amounted to 28.4 PJ, a 4% increase in absolute terms from 2003. However, after correction for a production increase of 10%, we realized a comparable decrease of 6% versus 2003.

Lighting and Semiconductors share equally the 86% of total energy used in our production processes. A comparable decrease of 6% was realized as two of Lighting's largest factories replaced their glass furnaces with more energy efficient ones, and a third phased out an energy-intensive chemical etching process. Further, one of our Semiconductors facilities reduced energy consumption by changing their cleanroom concept.

The comparable decrease in energy consumption at company level was 26% against 2001, surpassing the 10% target.

In 2004, 76% of all energy consumption was purchased as electricity, up 2% from 2003. Gas dropped to 20%, a decrease of 1% compared to 2003.

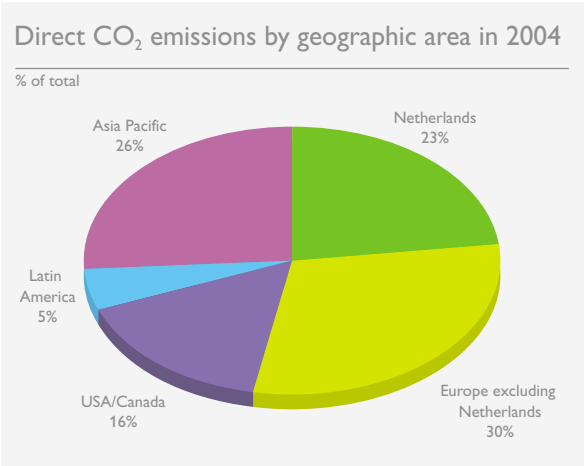
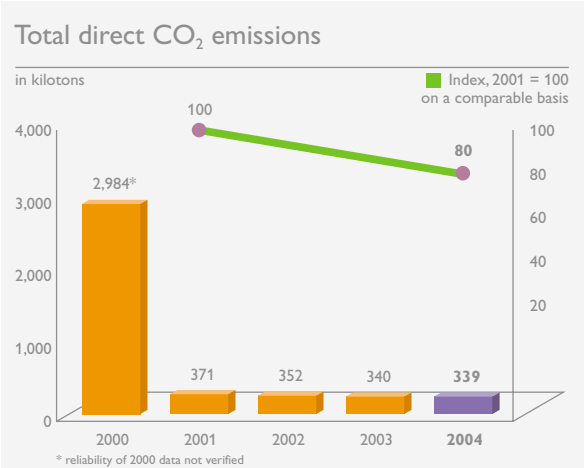


CO<sub>2</sub> emissions

Direct CO<sub>2</sub> emissions from production in 2004 amounted to 339 kilotons compared with a comparable 340 kilotons in 2003. Of these emissions the glass furnaces of Philips Lighting contribute 77%.

CO<sub>2</sub> equivalents

In our 2003 report we stated that we would adapt our reporting systems to include the global warming effects of Per Fluorinated Compounds (PFCs) from our Semiconductors division. Philips emits 885 metric kilotons of CO<sub>2</sub> equivalents mainly in the form of PFCs. Calculations are based on the mechanisms developed by the Semiconductor Industry Association.

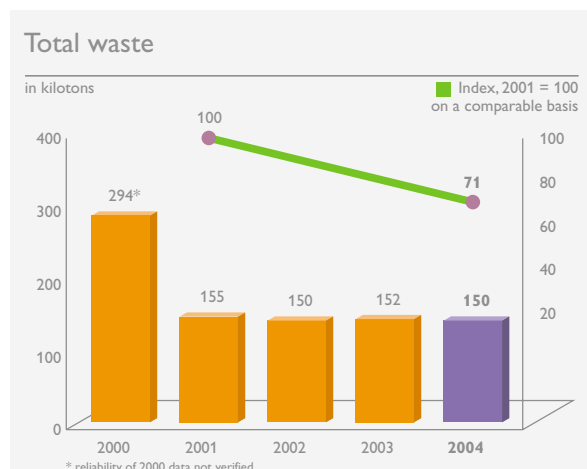


### Waste

We make a distinction between recycled waste (material explicitly delivered for secondary use) and actual waste (waste not delivered for secondary use and disposed of by landfill or incineration). Total waste is made up of actual waste that is delivered for either landfill or incineration, and recyclable waste.

Globally, Philips promotes methods to reduce waste generation and considers landfills a last resort. The EcoVision program targets a 20% reduction in total waste.

Philips disposed of 150 kilotons of total waste in 2004 – a slight decrease in absolute terms compared with 2003. We exceeded our EcoVision target of a 20% comparable total waste reduction, achieving a 29% decrease for the company as a whole. Both Lighting and Semiconductors achieved a 12% comparable reduction in 2004 versus 2003. Lighting (with a 56% share of total) achieved a 31% comparable decrease against 2001, and Consumer Electronics and Semiconductors achieved a combined 36% comparable reduction against the base year 2001.

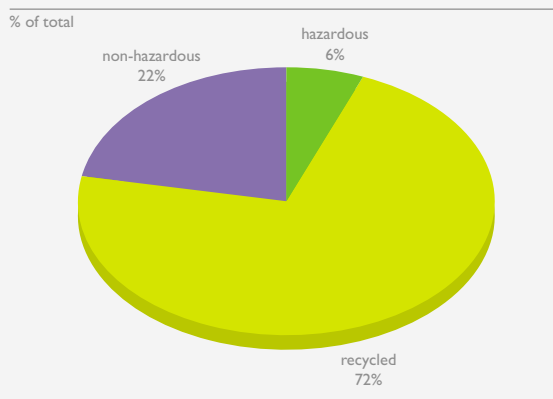


In 2004 actual waste was comprised of 22% non-hazardous and 6% hazardous waste, with the remaining 72% (or 107 kilotons) delivered to recycling companies.

## Water reuse

Water use is a significant issue in semiconductor manufacturing. That's why Philips Semiconductors Philippines in Cabuyao Laguna has developed a system to recycle final rinse water used in its polishers. To do this, the facility operates two systems – one is on standby while the other is in service. Before this change, water was discharged for wastewater treatment. Now it is recirculated until the system is serviced. This saves on both water and chemicals, as the water is no longer treated. This project enables us to save 244 m<sup>3</sup> per month.

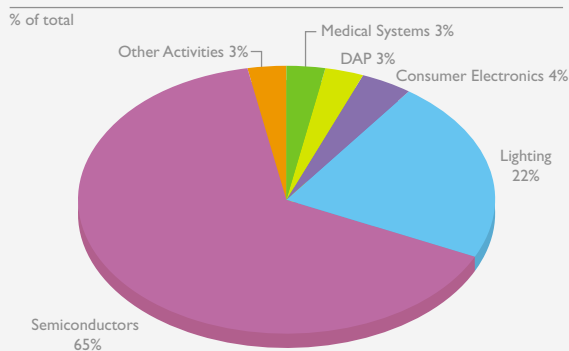
### Composition of total waste in 2004



### Water

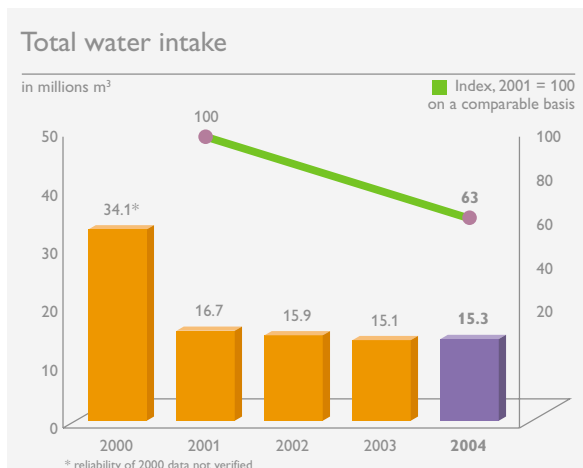
Water plays a critical role in electronics production processes, particularly in the manufacture of semiconductors, which requires large volumes of ultra-pure water. The company continues to be committed to using water responsibly, and has targeted a 15% reduction in water usage by year-end 2005.

### Total water intake by sector in 2004





Lighting and Semiconductors account for 87% of our total water consumption. The amount of water used in 2004 (15 million m<sup>3</sup>) increased 1% in absolute terms compared to 2003. Through more efficient use of water, Lighting achieved a 13% comparable reduction versus 2003. Philips as a whole exceeded the EcoVision program target by 12%.



#### Management of chemical substances in production

Our policy identifies three categories of chemical substances and provides instructions for their management:

- **Category I** – restricted substances, such as benzene and mercury, the use of which Philips has restricted in production worldwide because they are considered most harmful to the environment. Within this category, certain substances have been banned: cadmium, polychlorobiphenyls, polychloroterphenyls and halogenated hydrocarbons (CFCs, CHCs, HCFCs). Restricted substances should only be used where no alternatives are available, and require a formal internal waiver.
- **Category II** – hazardous substances, such as arsenic, cyanides and lead, the use of which is not forbidden, but must be reduced as much as possible, based on the most cost-effective, technologically feasible method.
- **Category III** – relevant substances, such as nitrates, phosphates and boron, the use of which has to be reduced in keeping with the principles of good housekeeping and ISO 14001. These substances have the smallest impact on the environment, but in most cases these substances are emitted in the largest quantities.

All substances in each category are listed in full on page 105.

## Eliminating acetone

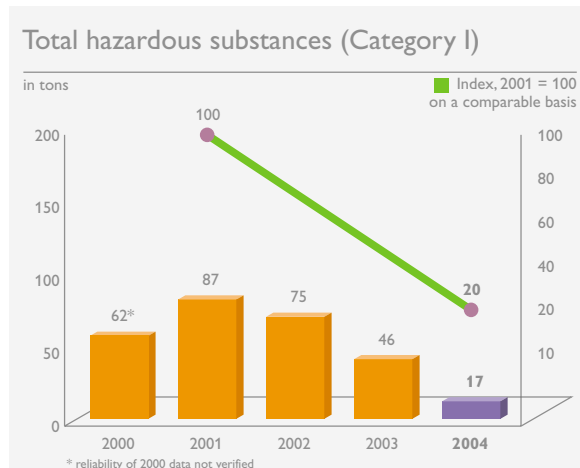
Philips Lighting Shanghai eliminated the use of acetone for dipping electrodes, replacing it with a non-volatile environmentally friendly liquid. While this substance is more expensive than acetone, less is required so the total cost is nearly equal to acetone. Prior to this project, the facility used 400 kg of acetone annually.

#### Emissions to air and water

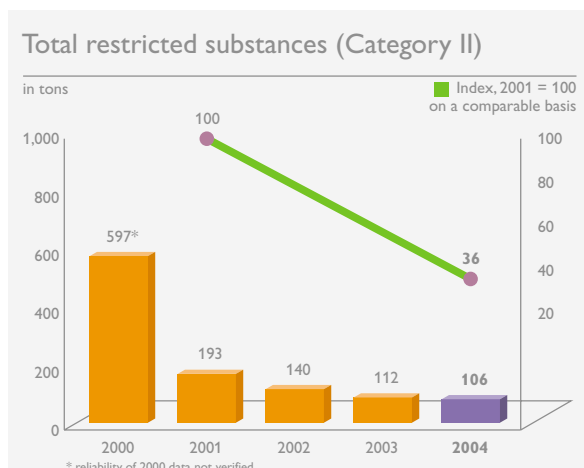
Philips conducts investigations to reduce the quantity of harmful substances in use to an absolute minimum without adversely affecting product specifications.

Our 2004 production activities resulted in the following emissions:

- 17 tons of Category I (Restricted Substances) – a 63% decrease in absolute terms compared with 2003. More than 80% of is attributable to Semiconductors Shanghai's 67% reduction in Category I emissions because of a shift to a water-based process. On a cumulative basis for the company as a whole, a comparable decrease of 80% has been achieved against the base year 2001.



- 106 tons of Category II (Hazardous Substances) – a 6% decrease in absolute terms compared to 2003. Semiconductors is responsible for 76% of all Category II emissions due to PFCs. Lighting's 11% Category II emissions is due to xylene and toluene (used in wet painting processes). The comparable decrease against the base year 2001 is 64%

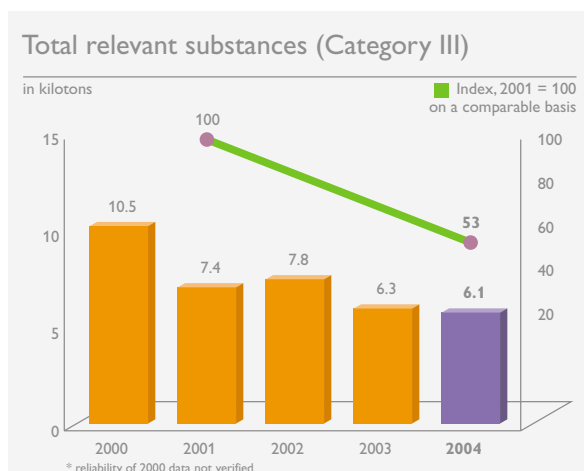


In 2004, 19 incidents were reported in six categories. They were related to waste (one), water (seven), soil (four), fire (two) and emissions of Category I (three) and Category III substances (two).

#### Other operations

Although the major environmental impact of our facilities lies in production, in 2002 we identified our non-industrial facilities, such as offices, logistic centers and R&D. The decision on reporting on non-industrial activities will be made in 2005 when we establish our new EcoVision 2005-2009 program.

- 6,122 tons of Category III (Relevant Substances) – a 2% decrease in absolute terms compared to 2003. Lighting and Semiconductors combined account for 96% of the total use of Category III emissions. The comparable decrease versus the base year 2001 is 47%



#### Legal compliance

Compliance issues are resolved through local management with legal counsel.

For information about provisions for environmental remediation please refer to page 137-138 of the Annual Report 2004.

In 2004 Philips incorporated the registration of fines related to non-compliance issues in its reporting systems. An amount of EUR 20,276 was reported.

#### Incidents

Environmental incidents are unintentional events that may have adverse effects on the environment. They can be caused by human error, technical defects or natural disaster.



## Driving business growth with sustainable solutions

Philips Lighting customer Johnson Controls, Inc., has a sharp focus on sustainability. Paul von Paumgarten, Director of Energy and Environmental Affairs at Johnson Controls, sees sustainability as a serious business issue.

People often think 'green design' is expensive, but lighting is a key example of a product line that doesn't necessarily cost more when used in an integrated design system, such as those described in the US Green Building Council's (USGBC) Leadership in Energy & Environmental Design for Existing Buildings (LEED®-EB) regulations.

The USGBC is a coalition of leaders from across the US building industry working to promote buildings that are environmentally responsible, profitable, and healthy places to live and work. LEED-EB is a set of performance standards for the sustainable operation of existing buildings that encourages exceptional, long-term performance.

Philips Lighting in the US announced a three-pronged approach in November 2004 to help commercial customers meet LEED-EB regulations with use of lighting in their buildings through the company's:

- wide array of low-mercury and energy efficient products
- online sustainable lighting index calculator; and
- Innovations Roadshow educational series on sustainable lighting.

### Low-mercury product mix

Philips set the industry standard in green-lighting practices 10 years ago with the creation of its low-mercury ALTO lamp technology (see page 65), and has produced more than 1 billion ALTO lamps.

### Online tool for customers

Existing buildings must have a maximum of 100 pico-grams per lumen output to pass the LEED-EB standards. By offering its wide array of low-mercury products, Philips exceeds this standard with a goal of achieving 80 pico-grams per lumen output. To determine the mercury content and the environmental impact of their buildings, customers can measure their performance online using the Philips Lighting sustainable lighting index calculator.

### Seminar series

We began our Innovations Roadshow program in 2002, hosting a series of educational seminars in locations around the US. The program grew in 2003 as it gained

accreditation by the American Institute of Architects and continued in 2004.

During the year, Philips also joined other global corporations to form the Alliance for Sustainable Built Environments. Founding members Johnson Controls, Inc., Philips, Forbo Flooring, Johnson Diversey and Milliken Carpets along with new member Owens Corning are working to use their cumulative knowledge and expertise in emerging sustainable solutions and technologies to bring cost-effective and environmentally beneficial strategies to businesses.

Each of the companies in the Alliance is committed to providing products and services that increase environmental performance. "Together we can serve as a market catalyst and accelerate the marketplace toward constructing and operating sustainable buildings," explains Paul von Paumgarten, Director of Energy and Environmental Affairs at Johnson Controls, which is a Philips customer and partner in the Alliance.

Johnson Controls is a global market leader in automotive systems and facility management and control. Philips is the exclusive supplier of all lamps and ballasts for Johnson Controls, according to Von Paumgarten. "We want to work with companies that have similar values to ours. And we find that Philips has a true organizational commitment to sustainability. It shows in the products and services, the marketing and manufacturing, and in how Philips educates internally and externally," he says.

"This is a serious business issue," he notes. "Initial analysis indicates that energy efficient buildings save money – the financials are very compelling – with just a one or two year payback. We believe that companies that provide these solutions will prosper as this LEED for Existing Buildings takes hold."







# Economic responsibility

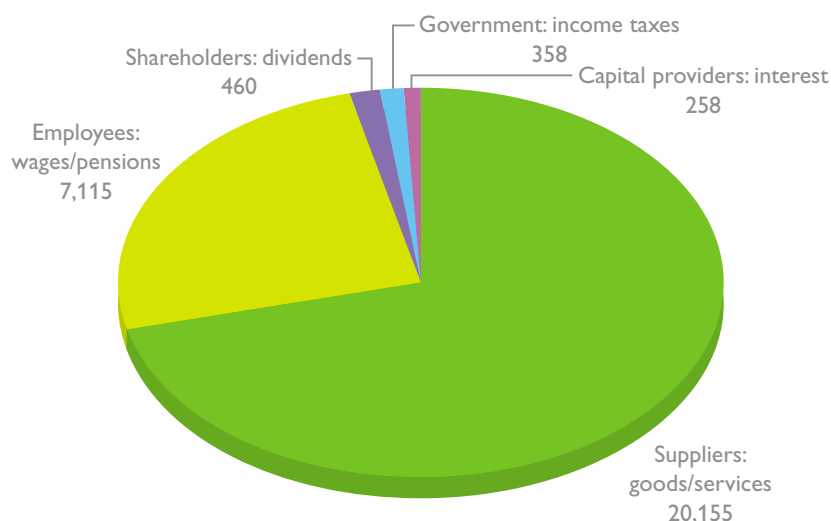
Sustainability is how we do business. We have long been integrating economic prosperity, environmental quality and social equity – balancing these sometimes-competing demands with a clear view on sustainable value creation.

2004 was a year of major progress for Philips. Driven by our focus on operational performance and cost management, our financial results showed considerable improvement, delivering a return well in excess of our cost of capital. Going forward, however, our focus on innovation is providing Philips with a basis for stronger growth across all our divisions.



## Distribution of economic benefits 2004

in millions of euros



### Economic stakeholders

From a societal perspective, the economic performance of our company goes beyond the traditional performance indicators such as profitability, balance sheet ratios and cash flows. It covers the various components that represent the cash outflow to all economic stakeholders. They can be mapped in the following chart, which illustrates the mega impact of our suppliers in relation to all other economic stakeholders, all expressed in terms of cash flow.

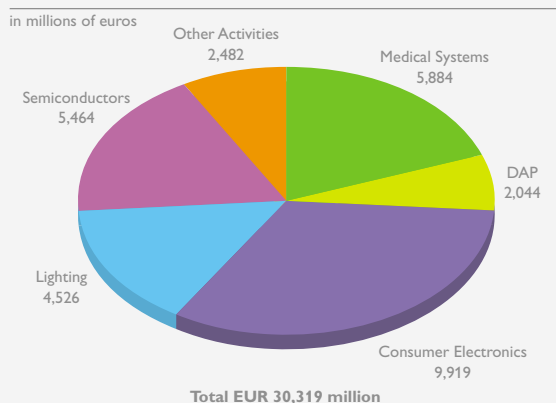
### Customers

Our sales in 2004 amounted to EUR 30,319 million compared with EUR 29,037 million in 2003, an increase of 4% nominally. The reduced value of the US dollar and other currencies had a 5% negative impact on sales in 2004. Adjusted for this negative currency effect, comparable sales were up by almost 9% compared to 2003.

The 4% increase in comparable sales at Medical Systems was driven by double-digit growth within computed tomography (CT) and X-Ray. At Domestic Appliances and Personal Care (DAP), an increase in sales at Food & Beverage and Shaving and Beauty was offset by lower sales at Oral Healthcare and Home Environment Care. At Consumer Electronics (CE), Connected Displays, Mobile Infotainment and Licenses drove the 11% comparable sales growth. The 5% comparable increase at Lighting was due to higher sales in all businesses, mainly driven by innovation. Semiconductors excluding Mobile Display Systems (MDS)

showed comparable growth of just below 20%, the main driver being Mobile Communications. Within Other Activities, sales growth came predominantly from Optical Storage.

### Sales per sector 2004



### Geographic sales distribution

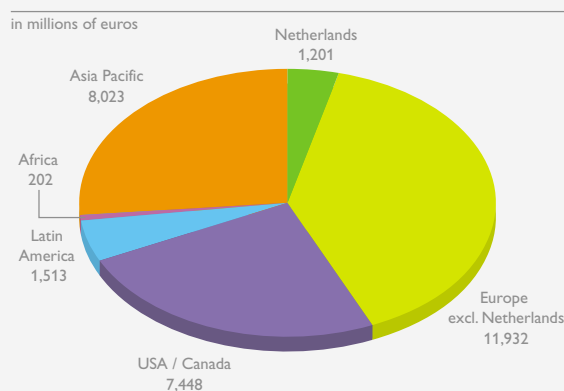
Our sales in 2004 in Europe grew by 4%, as divestments and weaker currencies (e.g. the pound sterling) had a 1% downward effect. All sectors except DAP recorded sales growth, led by Semiconductors, Miscellaneous and CE.

Our sales in North America decreased by 6%, almost entirely because of the weaker US dollar. On a comparable basis, sales increased by 3%. This was attributable to all sectors except DAP.

Sales in Latin America increased by 32% on a comparable basis and growth was visible across all targeted countries and most product divisions.

Sales in Asia Pacific increased by 13%, hampered by the negative effect of weak US dollar-related currencies. On a comparable basis, our sales grew by 17%, headed by sales in China (25% comparable growth). Excluding the effects of changes in consolidations and currencies, double-digit growth was visible across every product divisions except Medical Systems and DAP, which both grew by 8%.

#### Sales by geographic area 2004



### Employees

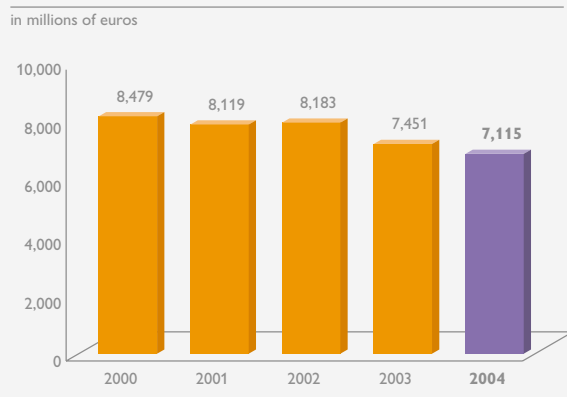
#### Wages

The composition of our workforce and the changes in 2004 has been addressed in the employee section of this report.

The economic benefits for our employees are the direct and indirect wages. The total amount of wages in 2004 amounted to EUR 7,115 million and was composed of the following elements:

	in millions of euros
Direct salaries and wages	5,932
Pension costs	284
Other social security and similar charges	
Required by law	769
Voluntary	130
<b>Total</b>	<b>7,115</b>

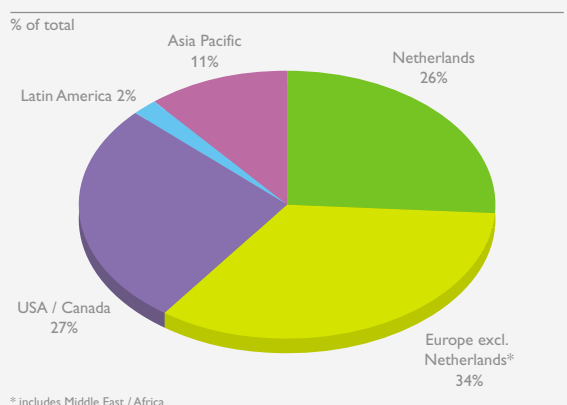
#### Total wage bill development



The total wage bill decreased 4.5% in 2004, compared with the year before. The main reasons for this decrease are:

- The reduction of pension costs, mainly due to a renegotiated pension arrangement in the Netherlands, from EUR 442 million to EUR 284 million in 2004
- A decrease in social security and similar charges that are required by law from EUR 851 million in 2003 to EUR 769 million in 2004
- Weaker currencies (close to 40% of our wages are paid in the USA and dollar-related areas)
- The decrease in the number of our employees (0.6% on average basis)
- The further shift of production and assembling activities to Asia Pacific.

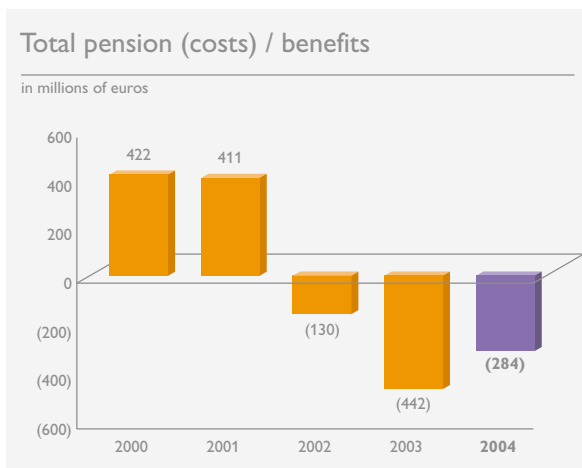
#### Wage bill per geographic area in 2004



Employee pension plans have been established in many countries in accordance with legal requirements, customs and local conditions. The majority of employees in Europe and North America are covered by defined-benefit plans. The benefits provided by these plans are based primarily on employees' years of service and compensation near retirement. Contributions are made by Philips, as necessary, to provide assets sufficient to meet the benefits payable to

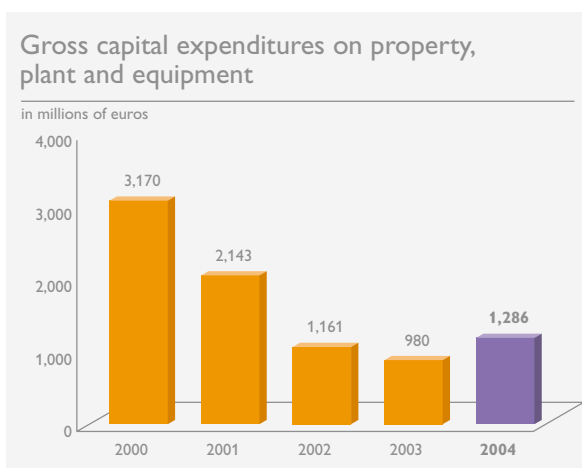
defined-benefit pension plan participants. In addition, we sponsor defined contribution and similar plans for a significant number of employees, with a total cost of EUR 54 million in 2004.

After strong increases in total pension costs between 2002-2003, a reverse trend was posted in 2004, resulting from the renegotiations of pension arrangements in the Netherlands.



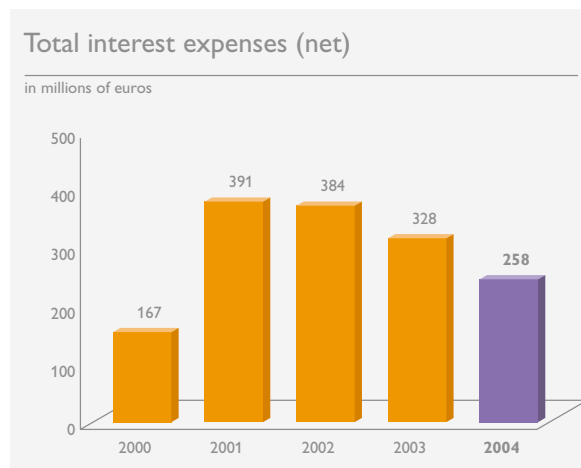
### Suppliers

Total products and services purchased in 2004 amounted to EUR 20 billion, representing 66% of total sales. One of the components of the total amount relates to Gross Capital Expenditures on property, plant and equipment. After three years of decline, these expenditures increased in 2004, totaling EUR 1,286 million. The increase relates primarily to Semiconductors, in particular caused by the SSMC, which was not consolidated previously. In addition, an amount of EUR 103 m. was paid for intangible assets (software etc.).



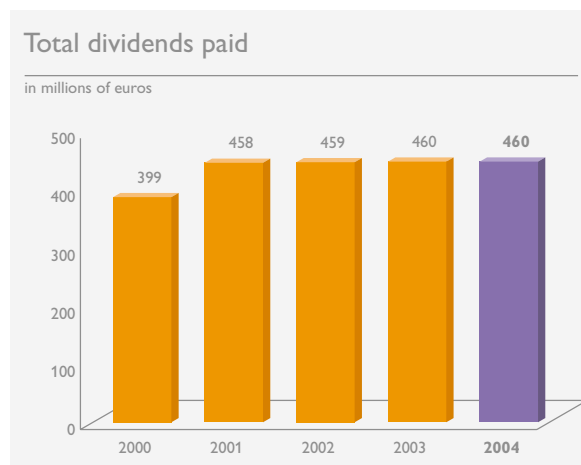
### Providers of capital

The total net amount of interest expenses decreased further in 2004 to EUR 258 million, as a result of a significant decrease in net debt.



### Dividends

In 2004 an amount of EUR 460 million or EUR 0.36 per common share was paid as dividend to shareholders, unchanged from previous years. A proposal will be submitted to the General Meeting of Shareholders to declare a dividend of EUR 0.40 per common share (EUR 513 million).



### Financial performance in 2004

Net income amounted to EUR 2,836 million in 2004, following a profit of EUR 695 million in 2003. The steep improvement is due to a better underlying performance at Semiconductors and Medical Systems and improved income from unconsolidated companies. A number of events had significant positive and negative impact on the financial performance of our Company. The events with a strong positive impact were the Initial Public Offerings (IPOs) of NAVTEQ and LG.Philips.LCD, the sale of shares of Atos Origin, Vivendi Universal and ASML, and gains



## Sustainability is a value-adding factor

By Robert Hassler

Robert Hassler is Chief Executive Officer of oekom research AG, an independent rating agency that provides in-depth information on the environmental and social performance of companies, sectors and states.

Sustainability-oriented companies are more successful economically than others. Our belief in this statement is strongly supported by a study we recently carried out in cooperation with Morgan Stanley. It shows that the share price movements of the companies we recommended for inclusion in sustainable investments have outperformed the share prices of those firms we explicitly did not recommend due to environmental and social shortcomings.

Between 2001 and 2004 the 'Best in Class' companies have outperformed their lagging counterparts by almost 17%. The outcome of our study backs the trend identified in many other analyses. It is becoming more and more widely recognized that sustainability is a value-adding factor. A growing number of financial service providers and investors share this opinion and include social and environmental research into their decision making process.

Worldwide, sustainable capital investments are growing at a fast, steady pace. By the end of June 2004, 354 green, social and ethical retail funds with EUR 19.0 billion of assets under management operated in Europe. Compared to June 2003, this marks a 13% increase in numbers, and a 57% increase with regard to assets under management.

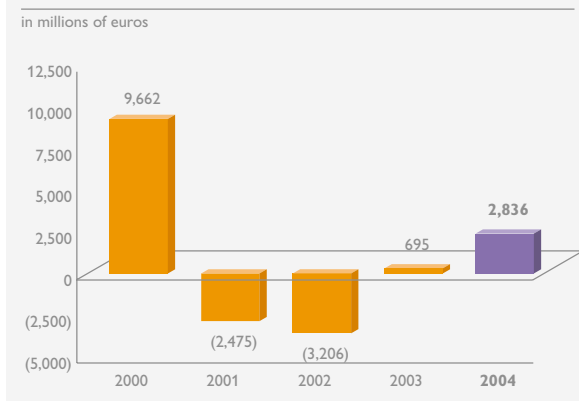
So far, three approaches offer possible reasons for the positive correlation of companies' financial and sustainability performance:

- A strong sustainability performance results in a strong financial performance. By integrating sustainability criteria into the corporate strategy, companies enhance their value. E.g. companies cut costs through higher efficiency of energy and raw materials.
- The second approach brings forward the argument that a strong financial performance results in a strong sustainability performance, meaning that companies with higher profits can afford higher environmental and social standards – a fact that can hardly be denied.
- Finally, the third approach indicates that companies with a strong sustainability performance feature an overall superior management that results in a better financial performance. Therefore, a strong management results in a strong financial and sustainability performance.

In order to determine which approach hits the mark, oekom research has started a project with the University of Munich that analyzes which factors show a significant contribution to the overall correlation.

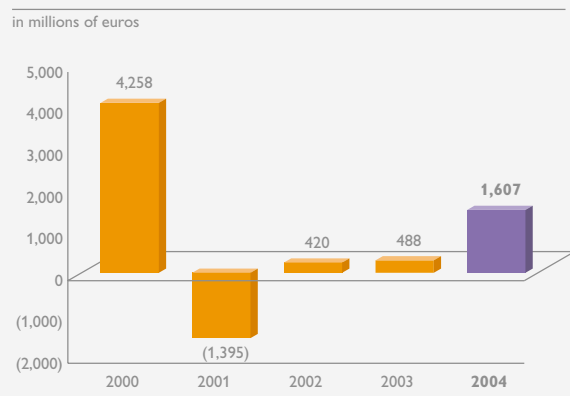
associated with transactions by Atos Origin and InterTrust. The total positive effect of these events was EUR 1,590 million on net income. The events with negative financial consequences were the impairment charge for MedQuist and the litigation settlement for Volumetrics, which had an impact of EUR 676 million on net income.

### Net income (loss)



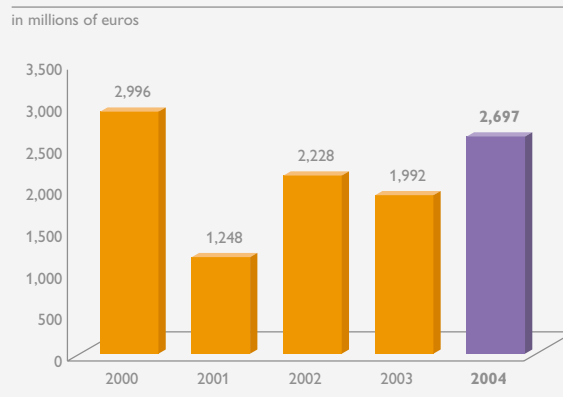
Income from operations increased to EUR 1,607 million, or 5.3% of sales, moving closer to our goal of a 7-10% operating margin, to be realized within one to two years from now. The improvement is attributable to improved market conditions, higher-margin products from innovation and continued tight control of costs. Income from operations included a gain from the initial public offering of NAVTEQ (EUR 635 million) as well as an impairment charge for MedQuist (EUR 590 million) and the cost of settlement of litigation with Volumetrics (EUR 133 million).

### Income (loss) from operations



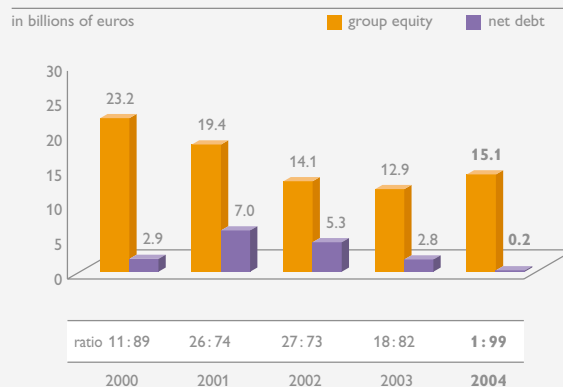
Cash flow from operating activities improved considerably to EUR 2,697 million in 2004, from EUR 1,992 million in 2003. Inventories as a percentage of sales at the end of 2004 amounted to 10.7%, a record-low.

### Cash flows from operating activities



Stockholders' equity increased by EUR 2,097 million. On a net basis, our company is now virtually debt-free, which will allow us to pursue our growth plans.

### Net debt to group equity



### Public sector

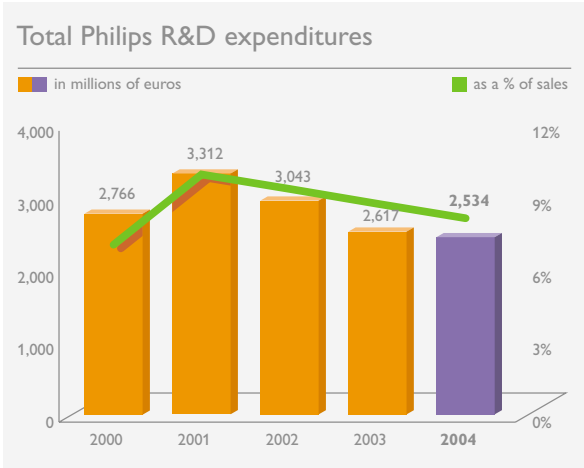
Income taxes represented a charge of EUR 358 million, compared to a benefit of EUR 15 million in 2003. Excluding non-taxable gains on the IPO of NAVTEQ and the selling of shares in Vivendi and ASML and the non-tax deductible impairment relating to MedQuist, the tax rate in 2004 corresponded to an effective tax rate of 27%, compared with an effective tax benefit of 6% in 2003. Next to these income taxes that are paid by the Company, there is an additional effect of income taxes that are paid by the employees, as part of their income.

In addition to income tax, our organizations across the world pay various taxes and licenses to local authorities. These amounts are not reported separately in the corporate consolidation system.

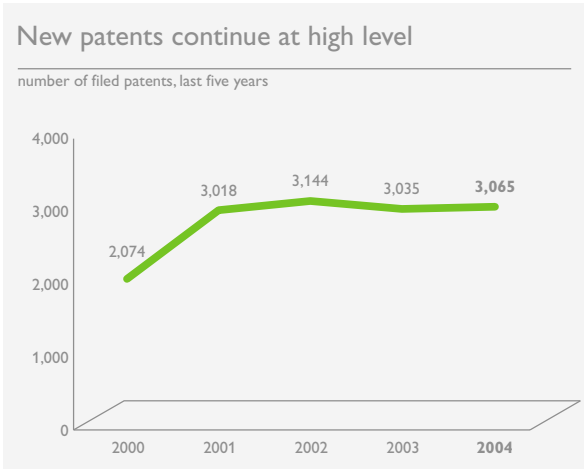


Technology

R&D expenditures totaled EUR 2,534 million in 2004, representing 8.4% of our sales, slightly below the 2003 level.



Despite slightly lower R&D expenditures we maintained our high level of first filings of patents. In 2004 we filed 3,065 new patents. By year-end 2004 the total number was 115,000.



# Our suppliers

With our own deep commitment to sustainability, we encourage active cooperation and initiatives from our supply base.

The objective is to have a consistent approach throughout the supply chain to promote a high level of sustainability also in the extended business system. To manage this complex issue we have introduced a comprehensive program with tools and feedback mechanisms for our supply base.

In the electronics industry the importance of supplier management is fueled by the increasing percentage of components and products that are purchased rather than manufactured in-house. This creates an interdependency that needs to be managed well to benefit both Philips and its suppliers. As the total amount of products and services purchased in 2004 of EUR 20 billion, or 66% of our total sales, it is clear that supplier management is of significant importance.

## From purchasing to supply management

The dynamics of the Philips supply base are changing – nearly 80% now comes from outsourcing, long-term partnerships, Original Equipment Manufacturers (OEM), Original Design Manufacturers (ODM) and products or services that our product divisions can buy together. The remaining 20% of our bill of materials spend comes from traditional purchasing – buying raw materials and components for our own manufacturing purposes.

In our changing business, the focus is on semi-finished and complete products. The challenge is to run a flexible, lean and 'virtual' product manufacturing model in a market that depends on speed, total cost of ownership and reliability of products and services. In answer to these dynamics, our Chief Procurement Officer, who is a member of the Group Management Committee, and the Philips Purchasing Leadership Board have defined a clear mission for Philips Purchasing to transform purchasing into supply management and extract the 'Power of One Philips' by leveraging our combined purchasing power.

To realize this mission, Philips is focusing on a concentrated group of suppliers who are in alignment with our company strategy. In this context Philips initiated its first Global Supplier Forum in 2004, which was discussed on page 23.

## Sustainability and supplier management

This mission, combined with a considerable supply base in Asia and Central and Eastern Europe, calls for a common, responsible management approach based on a shared set of values and principles.

That's why we developed in 2003 the 'Supplier Sustainability Involvement Program,' which is comprised of three steps:

- creating awareness by communicating about our Philips Supplier Declaration on Sustainability
- setting out basic principles of responsible behavior, further enhancing awareness with a self-assessment and sustainability workshops,
- and, where deemed necessary, following with assessments performed by Philips qualified assessors or third-party auditors, as part of our One Philips certification process.

This program is being developed and executed in keeping with our Supplier Sustainability Platform consisting of supply management and sustainability representatives from all of our product divisions, supported by the Corporate Sustainability Office. This team is responsible for embedding sustainable performance in all supply base processes and procedures, as well as strengthening our supplier sustainability program.

## The Philips Supplier Declaration on Sustainability

The Philips Supplier Declaration on Sustainability was sent at the end of 2003 and early 2004 to our key suppliers, as well as those in countries we perceive to have a higher risk factor, given earlier studies done in the area of child labor. The declaration outlines the minimum expectations of behavior in the areas of environment, health and safety, and labor conditions, including child and forced labor. Adhering to these requirements, either by accepting this declaration or by confirmation of adherence to similar sustainability programs, has become an important factor in the company's decision to maintain business relationships. We distributed the Declaration to an initial group of about 2,800 key suppliers, and all agreed to adhere to the principles set out in the document.

As a next step, we rolled out a supplier self-assessment tool in 2004 to this initial group of suppliers. Suppliers have been invited to perform the self-assessment to provide them with insight into their social and environmental performance. They can complete an electronic

# Sustainability workshops for suppliers



We are pleased with the response to our Supplier Declaration on Sustainability, but we also know it is not enough. We have identified the need to help, support and educate our suppliers on sustainability in a proactive way. That's why we are organizing our sustainability workshops in all relevant regions of the world, to train and support our suppliers in achieving and maintaining compliance to our sustainability requirements.

The first Consumer Electronics Sustainability Workshop was held at our Suzhou plant in June 2004. More than 50 local suppliers were invited, with participants including general managers and directors. Topics discussed included the Philips Sustainability Policy, the sustainability agenda, the company's sustainability organization and supplier involvement.

## Suppliers get on board

Suppliers showed their shared commitment by signing the Philips Supplier Declaration on Sustainability. They performed a Supplier Sustainability Self-Assessment, brought real-world challenges into the discussion and worked to come up with possible solutions. For example, the group that focused on health and safety discovered that some new employees have no strong concept of safety in their workplace. One suggestion discussed was for that company to provide new hires with an orientation covering health and safety as well as on the job training.

Subsequent sustainability workshops were held in Manaus, Brazil; Szekesfehervar, Hungary; in the Chungli, Taiwan; Dalinshan and Shenzhen, China; Pune, India; and in Juárez, Mexico, in early 2005.

questionnaire or can conduct a self-assessment during sustainability workshops.

## Supplier assessment and certification approach

In a joint effort between various staff functions and the product divisions, Philips developed a supplier assessment and certification process, supported by a standardized supplier assessment and selection tool, a common assessor training program and an aligned contractual baseline for new suppliers. Sustainability criteria have been integrated in these instruments for measurement and compliance monitoring processes.

Further, to ensure inclusion of new suppliers in the Supplier Inclusion Program, the supplier selection processes have been redesigned to include social and environmental performance up to par with the content of our Supplier Declaration on Sustainability as a precondition for selection.

With these tools in place, we started the first supplier assessments in 2004. Supplier certification reviews for key suppliers are performed under the supervision of qualified internal auditors or selected external auditors. More than 100 Philips managers have taken the supplier assessment training, which will enable us to conduct supplier assessments on a larger scale in 2005.

In line with the Philips General Business Principles and related procedures, all material non-compliances encountered during supplier assessments are required to be reported to Philips Compliance Officers and included in the global non-compliance database for monitoring and cross product division information exchange. Initial supplier assessments have led to corrective action plans with a number of suppliers and the phasing-out of at least one supplier.

## Monitoring sustainability supplier management

One of the tools to help us in measuring and continuously improving our performance is the sustainability maturity grid for the Supply Management discipline.

The maturity grid on the next page is a ladder of statements with increasing quality demands towards sustainability world class. By identifying the statement applicable to the organization, that organization determines its quality level and can define action plans to get to a next step on the ladder.

Reporting on our maturity level began in mid-2004. The aim is to have reporting implemented to the lowest organizational level. Consolidated validation takes place per product division as part of internal control procedures. The reporting system is user-friendly and supports a standardized way of working. While we intend to report verified data on these parameters, as the collected data

## Sustainability maturity grid

Step 13	Demonstrable world class level versus peers <sup>*)</sup> achieved	A
Step 12	Implementation of Benchmark results established	
Step 11	Benchmark against peers <sup>*)</sup> on policy content and performance management aspects	
Step 10	100% of assessed suppliers has implemented corrective action plans	
Step 9	Assessed results evaluated and improvement plans established	B
Step 8	Assessments carried out according to plan	
Step 7	Assessment plan and frequency established for short listed suppliers	
Step 6	Methodology and criteria applied; short list for assessment purposes established	
Step 5	Objective methodology and criteria for assessment selection defined and documented	C
Step 4	> 80% feedback received from suppliers	
Step 3	Policy communicated to and feedback asked from suppliers	
Step 2	List of Suppliers established	
Step 1	Policy and consequences for non-compliance/non-respondents established	

<sup>\*)</sup> Peers of external comparable industry group per division

does not yet meet our standards of reliability that information is not included here.

### The focus for 2005

In 2005 we will focus on assessing our suppliers as part of the Philips Supplier Certification Program that requires all new suppliers to go through a sustainability process with us.

Acting as One Philips organization is a major target of our supply management transformation process. Cross-product division programs with external auditing companies and audit training for our employees will be a major part of these activities.

Training of our supply managers and other employees on dealing with non-compliance is also part of this program. Joint sustainability improvement programs with the suppliers will be encouraged.

We will also roll out the Philips Global Supplier Rating System throughout the company. Currently in use in Optical Storage, Lighting and Consumer Electronics, this web-based system enables us to track our suppliers on six key dimensions: quality, delivery performance, cost, responsiveness, innovation and sustainability. Using a phased-in approach, we will first use the system to monitor sustainability performance with critical suppliers. Suppliers also will have access to the system, enabling them to get continuous feedback on their performance.

The Supplier sustainability management program will be further extended with all new contracted suppliers and those suppliers with high risk related to sustainability issues.

## Striving for consistency and cost-effectiveness

Electronics Manufacturing Services provider Sanmina-SCI Corporation is a supplier for Philips Medical Systems and Philips Consumer Electronics. We talked to Sanmina about driving sustainability through the supply chain.



“We build products for well-known companies like Philips that have valuable brands to protect,” says Randy Furr, President and Chief Operating Officer of Sanmina-SCI. “It is very important for our customers to be confident that we are in compliance.”

To do that and drive consistency within the industry, Sanmina-SCI has worked with some of its customers to develop ‘The Electronic Industry Code of Conduct’ for Original Equipment Manufacturers, Electronics Manufacturing Services firms and Original Design Manufacturers.

### Higher standards

“Our Code addresses the Philips Supplier Declaration on Sustainability along with other issues,” says Carmine Renzulli, Senior Vice President of Legal and Human Resources for Sanmina-SCI. “It lays out how Sanmina

and other companies will operate – at higher standards than local laws in health and safety, environmental, child labor and other issues.” This is important, as more than half of Sanmina’s employees are in low-cost parts of the world where the implementation of local laws are often not up to the Code.

Sanmina stresses that it is not enough to simply have a code in place. “We audit ourselves against the Code with external auditors and are driving this to our suppliers,” Renzulli adds.

There is a concern, however. This work adds cost. “It’s an interesting challenge for us,” explains Furr. “Obviously we have to compete and we must be in compliance. But we can’t put practices in place that will drive up cost. The key is to balance pricing with these requirements.”



## Choosing the right approach

Paul Hohnen has worked intensively on global economic, development and environmental issues as a diplomat, international civil servant, Director of Greenpeace International, Strategic Director of the Global Reporting Initiative (GRI), and as consultant to the government, business and non-profit sectors. We asked him about the array of codes, standards and frameworks to drive sustainable development and corporate responsibility performance.

Are there really hundreds of voluntary codes, standards and tools on almost all aspects of environmental, human and social rights and responsibilities?

**PH:** Yes, and it's not surprising that many executives are experiencing "standards fatigue" – a sense of profound confusion about what tools and standards exist, how they apply, how their costs and benefits stack up, and how they relate. This is true wherever you are in the supply chain. As a purchaser, you must ensure you are doing business with responsible organizations. As a supplier, you must live up to your customers' codes while driving your own performance. There is a tension between pleasing shareholders and other stakeholders: everyone wants something different.

How do other sectors of society see it?

**PH:** NGOs and unions accept that it is the responsibility of governments to ensure that laws protecting human rights and the environment are in place and enforced, but tend to blame business for the fact that these laws are often inadequate or unevenly implemented. In general, there is skepticism about the value of voluntary initiatives and the concept of corporate social responsibility (CSR).

Is there anything on the horizon that might clarify the situation?

**PH:** Several developments in the coming year will shape the future of the concept of CSR.

- First, human rights issues will be examined in a report by the UN High Commissioner for Human Rights. This will summarize the responsibilities of business and identify tools it can use to understand and implement inter-governmental agreements. However, in a world where human rights are defined differently in different countries – all at different stages of development – it is hard to see how a one-size-fits-all approach can be adopted without support in the form of policies to provide market rewards for better behavior.
- Second, the question of how far it is possible to translate existing international commitments into practical tools

will also be brought into sharp relief when the International Organization for Standardisation (ISO) starts work on a guidance document on social responsibility. The ISO process, involving representatives from government, business, unions and NGOs, will test the capacity of these sectors to work together. It will also expose the gap between globally agreed standards on the statute books and actual practice on the ground, and raise the question of who should be responsible for closing this gap.

- Finally, the five-year high-level review of the UN Millennium Development Goals, scheduled to take place in September, will measure progress being made towards the various goals set by heads of government in 2000. These goals – including cutting poverty by half – are bold and necessary, and business must play a key role. But this can't happen without the right policy environment, and a generally accepted framework for measuring and rewarding progress.

What might be the outcomes of these events?

**PH:** In a best case scenario, corporate social responsibility could play a powerful, positive role in meeting the challenge of sustainable development by helping business focus on its potential to do good, and to work with other sectors of society.

In the worst case, however, the concept might be seen as a cynical means of passing off 'business-as-usual' practices as new contributions to sustainable development. If this latter scenario – already expected by many NGOs – is confirmed by events, the CSR acronym could deepen divisions among sectors of society and come to mean the 'case for swift regulation' of business.

Ultimately, however, these events and other developments will place further pressure on governments to implement their commitments on sustainable development and ensure that the necessary mix of carrots and sticks is in place meet them.



## Auditor policy

The Company maintains a policy of auditor independence, and this policy restricts the use of its auditing firm for non-audit services, in line with US Securities and Exchange Commission rules under which the appointed external auditor must be independent of the Company both in fact and appearance. The policy is laid down in the comprehensive policy on auditor independence published on the Company's website.

## Assurance assignment

We have asked KPMG to review our Sustainability Report 2004 to provide the readers of the sustainability report with a reasonable level of assurance on selected financial data and a limited level of assurance on selected environmental data and the other information in the report. The report, including the identification of material issues is our responsibility. KPMG decided to perform the activities as described in their assurance report.

As we realize that building sustainability into our business processes is an ongoing process and that the quality of data collection at our manufacturing sites, and data analysis and internal controls at product division and corporate level need to be further improved to produce reliable data for all parameters, we have not asked KPMG to provide assurance on the reliability of the data in this report, except for the data on total energy consumption, total water intake, total waste and total direct CO<sub>2</sub> emissions for the years 2001 to 2004.

We have also asked KPMG to perform the activities as listed in the section 'Environmental data' in the section 'Work undertaken and conclusions' of their Assurance Report on our packaging, category I, II and III emissions, and health and safety data to provide us recommendations for the improvement of the quality of the data and data management systems.

We will continue building sustainability into our business processes and improving the quality of information, including following up KPMG's recommendations on the quality of packaging, category I, II and III emissions, and health and safety data and data management systems. We anticipate that we will have the reliability of all information independently reviewed in the future.

# Assurance report

To the readers of the Philips Sustainability Report 2004

## Introduction

We have been engaged by Royal Philips Electronics (Philips) to review the Philips Sustainability Report 2004 (further referred to as The Report). The Report is the responsibility of the company's management. Our responsibility is to issue an assurance report on The Report.

## Context and scope

In The Report Philips describes its efforts and progress in relation to sustainability and reporting. Our engagement was designed to provide the readers of The Report with:

reasonable assurance on whether

- the data on financial performance, as specified in the section 'Work undertaken and conclusions' are properly derived from the 2004 financial statements of Royal Philips Electronics;

limited assurance on whether:

- the data on total energy consumption, total water intake, total waste and total direct CO<sub>2</sub> emissions for the years 2001 to 2004 are reliable;
- the other information in The Report is fairly stated.

## Standards and criteria

We conducted our engagement in accordance with the International Standard on Assurance Engagements (ISAE 3000): "Assurance Engagements other than Audits or Reviews of Historical Financial Information", issued by the International Auditing and Assurance Standards Board. Amongst others this standard requires that:

- the assurance team members possess the specific knowledge, skills and professional competencies needed to understand and review the information in The Report, and that they comply with the requirements of the IFAC Code of Ethics for Professional Accountants to ensure their independence;
- when providing limited assurance, which is a lower level than reasonable assurance, a negative form of conclusion is used. There are no generally accepted standards for reporting sustainability performance. Philips applies its own internal sustainability performance reporting criteria, derived from the Sustainability Reporting Guidelines of the Global Reporting Initiative and internal corporate guidelines for HSE reporting, as detailed on pages 86-87 of The Report.

## Considerations and limitations

Environmental, health, safety and social performance data are subject to inherent limitations given their nature and the methods used for determining, calculating and estimating such data. It is important to view the performance data in the context of the explanatory information provided on page 86.

To obtain a thorough understanding of the financial results and financial position of Koninklijke Philips Electronics N.V. ('Royal Philips Electronics'), the reader should consult the Philips audited Financial Statements for the year ended 31 December 2004.

## Work undertaken and conclusions

### Environmental data

For the reliability of the data on total energy consumption, total water intake, total waste and total direct CO<sub>2</sub> emissions for the years 2001 to 2004 we conducted:

- visits to 16 reporting organizations in Europe, Asia and North America to review systems and data;
- reviews of:
  - the data reported by all EcoVision reporting organizations;
  - the data validation processes at corporate and product division level;
  - the calculations made at corporate level;
  - the data trends in discussions with management;
  - the changes in the data management systems for the reporting organizations that were visited in the previous three years; and
  - the systems used to generate, aggregate and report these data.

**Based on the above, the data on total energy consumption, total water intake, total waste and total direct CO<sub>2</sub> emissions for the years 2001 to 2004 do not appear to be unreliable;**

### Financial data

We have reconciled the data on financial performance in the sections of the Sustainability Report 2004 listed below, with the audited 2004 financial statements of Royal Philips Electronics.

- The section 'Highlights' on page 9, excluding the information on patent filings and portfolio;
- The sections 'Participations' and 'Our legal and shareholder structure' on page 10;
- The section 'Economic responsibility', excluding the graph 'Wage bill per geographic area in 2004' on page 75 and the information on patent filings on page 79.

**Based on the above, the data on financial performance, as specified above are properly derived from the 2004 financial statements of Royal Philips Electronics, for which the independent auditors issued an unqualified audit opinion dated February 22, 2005;**

### Other information

For the other information in the report we conducted:

- a review of the systems and processes used to generate this information;
- a review of internal documentation and intranet sources;
- interviews with staff for the information on Green Flagships, General Business Principles, stakeholder dialogue, diversity and inclusion, health & safety and social investments;

Following our review we discussed changes to the draft Report with Philips, and reviewed the final version of The Report to ensure that it reflected our findings.

**Based on the above, the other information in The Report does not appear to be unfairly stated.**

### Commentary

Without affecting the conclusions presented above, we would like to draw readers' attention to the following:

Philips is strengthening its approach to stakeholder engagement. Reporting on progress in this area next year would contribute to the transparency of the sustainability report. We recommend further integration of stakeholder engagement in the reporting and assurance process.

Philips made progress in implementing a programme for standardized data collection and reporting of health and safety data throughout the company and intends to bring the quality of these data up to higher standards of reliability. We recommend that Philips pays specific attention to enhancing the quality of internal control procedures around data collection and reporting at local, divisional and corporate level.

Amsterdam, 23 February 2005

KPMG Sustainability B.V.

## Explanatory notes

This appendix includes additional information about the environmental and health and safety data referred to in this report in the sections titled Environmental responsibility and Our employees.

### Environmental Responsibility.

#### Reporting standard

All reporting instructions, including definitions, procedures, calculation methods, etc., are included in the web-based EcoVision reporting and validation system. A reporting manual will be made available on our external website during the first half of 2005.

#### Basis for reporting

The environmental data in this report have been provided by our environmental reporting organizations. The following consolidation criteria have been applied:

- Starting point is the total of the consolidated Philips activities, as used for the reporting of the financial performance provided in the Philips Annual Report 2004
- Environmental data are reported by each manufacturing activity, owned, rented or leased and managed by Royal Philips Electronics, with 50 people or more working in production, and which is consolidated for financial reporting by Royal Philips Electronics
- Data from companies acquired are included in the report as from the year following the year of acquisitions
- Data from companies disposed of are excluded in the year of disposal
- Data are reported and validated on a half year basis.

#### Definition of comparable change

Due to continuous changes in market demands, production activities fluctuate accordingly. Most environmental parameters we measure in an absolute way go up and down over time in parallel with these changes. Therefore, in making comparisons between different periods, we take these production fluctuations into account. When comparing aggregated data at divisional, regional and company level we also have to deal with the changing composition of our company in different reporting periods. This means that through investments, divestments or organizational changes at divisional, regional or company level, the composition of the aggregated levels may differ from year to year. To establish comparable changes for a certain parameter at aggregated levels, Philips has defined the term comparable change. Used throughout this report, comparable change is the percentage of change for the current reporting year, versus an earlier year, including production fluctuations and organizational changes. To describe trends, the wording 'comparable increase,' 'comparable decrease' or 'comparable reduction' are used throughout this report. They all are equal to the above defined comparable change.

#### Accounting for production fluctuations

Production fluctuations are taken into account by expressing the absolute value divided by a factor that characterizes those fluctuations. The production index is defined as the ratio of these factors in two reporting years. Philips reporting organizations are obliged to determine which factor is most reliable to express their production fluctuations during the action program EcoVision 2002-2005:

- Number of products
- Number of employees
- Sales figures or added value
- Total m<sup>2</sup> build surface at the premises.

In high volume manufacturing activities such as those of our Lighting or Consumer Electronics divisions, the number of products is usually the common choice. On the other hand, in a business like Medical Systems, the number of employees is often chosen. Sales figures, added value or m<sup>2</sup> is chosen in those situations where the volume of products and the number of employees is relatively low.

Relative changes for a parameter of a reporting organization between two reporting years, is calculated by dividing the absolute parameter in each year by the chosen factor as mentioned above, determining the difference, which then is expressed as the difference between a current year B and the comparison year A in a percentage called comparable change (CC). We use the following formula:

$$CC = \frac{[(\text{value year B} / \text{factor year B}) - (\text{value year A} / \text{factor year A})]}{(\text{value year A} / \text{factor year A})} * 100$$

or

$$CC = \left\{ \frac{(\text{value year B}) * 100}{(\text{value year A}) * PI} - 1 \right\} * 100$$

$$\text{in which PI} = \text{production index} = \frac{(\text{factor year B})}{(\text{factor year A})} * 100$$

#### Accounting for organizational changes

In order to provide a basis for calculating comparable changes at aggregated levels, such as divisional, regional or company level, for a reporting year versus a previous year; the structure of reporting organizations in previous years has to be made comparable with that of the reporting year. To do that, we apply the following principles:

- Absolute data for new reporting organizations that started reporting in the current reporting year; are added to the divisional and thus company totals of the previous years, with the same absolute figures per parameter as reported in the current reporting year.
- Absolute data of reporting organizations that were divested in the current reporting year are taken out of the divisional and thus company totals, including their historic data from previous years.
- Absolute data from previous years for reporting organizations that moved from one division to the other in the current reporting year; are removed from the old division and placed in the new division, to realize a comparable basis for the divisions involved. These interdivisional reorganizations obviously do not affect company totals.

#### Organizational changes in 2004

Changes in 2004 were:

- Semiconductors
  - The SSMC site in Singapore has been consolidated to the Philips Group as per February 1, 2004 backdated to January 1, 2004, while it was part of a joint venture in the years before. Their environmental data for 2004 are included in the product division Semiconductors and in the Philips group. Although data are available for the earlier years, trend and reduction calculations are not taken into account, following the general rules for investments and divestments.
  - The operation in Shenzhen is no longer marked as a consolidated Philips activity, since it has the status of a subcontractor. All data for this site have been taken out from the PD Semiconductors and Philips Group data.
  - A new Semiconductors reporting organization is Suzhou and new business unit is PSS.
  - Full-scale production at Caen stopped at the end of 2003 due to a fire, and a new pilot line was established in 2004.
- Consumer Electronics: Kwidzyn TV sold to Jabil in November 2004; Beijing closed.
- Lighting: closed Calcutta Lamps, La Garriga, Monroe, Taoyuan; new is Ho Chi Min city.
- Medical Systems: new units are Best LRS and Veldhoven PMRS.
- Other Activities: Philips Optical Storage Wetzlar sold April 1, 2004, BU RF Solutions and Tuners merged and now called Solutions, PBC no longer fulfill criteria to report.

#### Accuracy

- The methods of determining environmental data carry inherent limitations with respect to accuracy. In a number of cases, reporting organizations had to estimate data.
- Reliability of packaging data need further improvement in view of mixed reporting activities between Reporting Organizations (ROs) and Business Units (BUs). Furthermore, it turned out that transport packaging is not always included in the reported data, although corporate definitions require it.
- Reporting on PFCs in the EcoVision data system has been more detailed for various substances, including specific conversion factors, which allows a more accurate calculation to the Global Warming Potential (GWP).
- (H)CFCs for coolants are likely to be underreported. However this has no material impact on the GWP data for the Philips group.

#### **Completeness**

- All reporting organizations reported on time. 159 out of 161 reporting organizations have been validated by the product division validators. The influence of missing data on divisional and corporate data is negligible.
- As our reporting organizations strive to improve the quality of our reported data, we have received a number of requests for data changes in absolute figures for previous reporting years, which we entered into our data systems to improve comparability. The materiality of these changes at Philips Group level is negligible.

#### **Comparability**

- In the year 2004 continuing efforts have been made to control the proper choice of type of factor, as described in the paragraph on production fluctuations, to determine the production index. We have learned that in some cases another choice would better reflect those fluctuations than the current one. However, we feel that comparable changes need further improvement in this area.
- As of the end of 2002, the Components division was dissolved and its activities were relocated to other divisions. The most important changes were the shift of the business group Mobile Display Systems to Semiconductors, while the business unit Optical Storage has been relocated to Other Activities. Reported data on environmental performance in 2003 and 2004 follows this new structure, which is in line with the financial reporting structure. The data for the years 2001 and 2002 have been restated. The absolute data for the year 2000, as they are included in the annexes, has not been restated.

#### **Green Flagship products**

- During the analysis of Green Flagships products 2004, we found that divisional EcoDesign procedures need further alignment. This will be an integral part of the measurement of EcoDesign maturity levels in the organization as described on page 61.

### **Health and safety reporting**

#### **Reporting standard**

All reporting instructions, including definitions, procedures, calculation methods, etc. are included in the web-based health and safety reporting and validation system. A manual will be made available on our external website during the first half of 2005.

#### **Basis for reporting**

- The Health & Safety data in this report have been provided by our reporting organizations, following the funloc structure that is also being used for reporting of financial data. Our scope of reporting is defined in our health and safety manual.
- Data are reported on a monthly basis and validated on a quarterly basis.
- Reporting of health and safety data for the Netherlands is conducted at a central level for all employees with a Philips contract.

#### **Accounting for organizational changes**

- Data for new reporting organizations that started reporting in the current reporting year are added to the divisional and thus company totals in the first quarter they are consolidated.
- Data for reporting organizations that were divested in the current reporting year are taken out of the divisional and thus company totals in the first quarter they are deconsolidated.

#### **Accuracy**

- The quality of reported data needs further improvement, particularly in applying the corporate definitions, since some organizations are used to report according to local definitions and requirements.
- Based on the 2004 data, we estimate that the reported lost work time rate is likely to be lower than actual, because of a possible over reporting of hours worked, combined with an under reporting of hours sick leave. In addition, we expect that the number of reported injury cases is below actual.

#### **Completeness**

- Data reported over 2004 cover 92% of the total number of Philips FTEs. The difference with the target of 100% can be explained by:
  - Non-reporting of MedQuist in the US, accounting for nearly 7,000 employees.

- Non-reporting for parts of the number of temporary employees in the Netherlands, being those that are hired via agencies.
- Under reporting of temporary employees in other locations.

#### **Comparability**

The year 2004 is the first year of reporting, no comparisons can be made with provisional data that have been reported in the year earlier.

## General Business Principles

### Introduction

Underpinning Philips' commitment to responsible corporate citizenship and the pursuit of a sustainable future – economic, social and environmental – the General Business Principles set out guiding principles on integrity and ethics in business conduct. They govern Philips' business decisions and actions throughout the world and apply equally to corporate actions and to the behavior of individual employees in conducting Philips' business. They are subject to applicable laws.

The General Business Principles are not all-encompassing, but formulate minimum requirements of behavior. They leave product divisions and country management free to specify further local rules of business conduct. To drive the practical deployment of the General Business Principles, a set of GBP Directives have been published, which are applicable to all employees. There are also separate Directives, which apply to specific categories of employees, such as the Financial Code of Ethics and the Purchasing Code of Ethics. The GBP Directives and the category-specific Directives form an integral part of the General Business Principles (jointly be referred to as 'GBP'). The General Business Principles, which have been adopted by the Board of Management and approved by its Supervisory Board, are reviewed on a regular basis and revised if necessary.

In order to ensure that business ethics are a living issue throughout the company, a worldwide training program is in place to heighten awareness of the absolute need for strict compliance with the General Business Principles.

December 2003

\* In these General Business Principles the expressions 'Philips' and 'Philips companies' are used for convenience and mean the Philips group of companies comprising Koninklijke Philips Electronics N.V. and its subsidiary companies.

### 1. General commitment

Philips' mission is to improve the quality of people's lives through the timely introduction of meaningful technological innovations. In a world where technology increasingly touches every aspect of our daily lives, Philips aspires to be a leading solutions provider in the areas of healthcare, lifestyle and enabling technology, delighting its customers with products and services that meet and even exceed their expectations.

Philips wishes to be a responsible partner in society, acting with integrity towards its shareholders, customers, employees, suppliers and business partners, competitors, governments and their agencies and others who can be affected by its activities. Philips duly observes the applicable rules of the law of the countries in which it operates and regularly reviews its interests and those of affected persons or entities in order to ensure a healthy, long-term relationship with them. Philips endeavors to adapt to local situations in order to take the most appropriate approach to possible problems within the bounds of applicable law and responsible conduct. In this respect Philips supports the principle of dialogue and cooperation with all parties involved.

#### 1.1 Human rights

With due regard to the Universal Declaration of Human Rights, which states that all parties in society, including corporate persons, have a duty to respect and safeguard human rights, and within the framework of the legitimate role of businesses, Philips supports and respects human rights and strives to ensure that its activities do not make it an accessory to infringements of human rights.

#### 1.2 Child, bonded and forced labor

Under no circumstances will Philips make use of forced or bonded labor; nor will it employ children in violation of Conventions no. 138 and no. 182 of the International Labour Organization.

#### 1.3 Free market competition

Philips supports the principle of free market competition as a basis for conducting its business and observes applicable competition laws and regulations.

#### 1.4 Product safety

Philips aims, at all times, to supply safe products and services.

#### 1.5 Privacy

The privacy of personally identifiable information about customers, employees, business partners and other individuals will be protected.

#### 1.6 Environmental protection

Consistent with Philips' commitment to sustainable development, it will do all that is reasonable and practicable to minimize any adverse effects of its activities on the environment.

### 2. Commitment towards customers

Philips is driven to improve people's lives. Its goal is to constantly delight each customer with breakthroughs both large and small. To this end, the company seeks to maintain an ongoing dialogue with its customers. Philips is committed to listen to and learn from them, so that it is able to design and deliver the solutions they really want and need. Philips will always deal with its customers in a fair and forthright manner, maintaining the highest levels of integrity.

### 3. Commitment towards shareholders

It is of central importance to Philips to conduct its operations in accordance with the highest standards of internationally accepted principles of good corporate governance. Philips aims to achieve a satisfactory return on equity, with the intention of maintaining a sustainable dividend payment to shareholders, while at the same time retaining sufficient funds in the company to generate profitable growth. Philips attaches great value to its relations with its shareholders and the financial markets and provides timely, regular and reliable information on its activities, structure, financial position and performance.

### 4. Commitment towards employees

Philips values its employees as a key resource. An atmosphere of good employee communication, involvement and responsibility is of central importance, and an employee's personal development and optimum use of talents is encouraged.

#### 4.1 Right to organize

Philips recognizes and respects the freedom of employees to choose whether or not to establish, or to associate with, any organization. Philips respects – within the framework of (local) law, regulations and prevailing labor relations and employment practices – the right of its employees to be represented by labor unions and other employee organizations, and Philips will engage in negotiations, either on its own behalf or through employers' associations, with a view to reaching agreement on employment conditions.

#### 4.2 Health and safety

Philips will do all that is reasonable and practicable to protect the health and safety of its employees.

#### 4.3 Equal and fair treatment

Every employee has equal opportunities and will be treated equally in employment and occupation regardless of personal background, race, gender, nationality, age, sexual preference or religious belief. The same applies to the recruitment of employees. Philips strives to offer equal pay for equal work performed at equal levels at similar locations. No form of harassment or discrimination will be tolerated.

#### 4.4 Wages and payment

Remuneration and working hours shall comply with local labor laws and shall at least be in line with prevailing industry norms.

### 5. Commitment towards suppliers and business partners

Philips pursues mutually beneficial relationships with its suppliers and business partners. It seeks to award business to suppliers and business partners who are committed to act fairly and with integrity towards their stakeholders and who observe the applicable laws of the countries in which they operate.



## 6. Assets and information

### 6.1 Use and protection of assets

Each employee is responsible for the proper use, protection and conservation of Philips' assets and resources as well as confidential information disclosed to Philips by its business partners. Philips' assets and resources as well as any opportunities arising by virtue of one's position, are to be used solely to pursue and achieve Philips' goals and not for personal benefit.

### 6.2 Improper disclosure

Philips regards information for the purpose of its business as a corporate asset that must be protected against loss, infringement and improper use and disclosure.

Philips is committed not to make use of information disclosed to it by a third party if it is suspected that the discloser thereby violates an obligation of confidentiality, unless the information:

- a. is generally available to the public other than as a result of disclosure by Philips;
- b. has been independently developed by Philips; or
- c. becomes available to Philips either on a non-confidential basis from a third party who is not bound by any confidentiality obligations or by operation of law.

### 6.3 Insider trading

All employees shall comply with Philips' insider trading rules. This means that non-public information which might influence the market price of Philips shares shall be kept in strict confidence until publicly released by authorized management. Furthermore, employees who have sensitive information which could influence the price of Philips shares and related rights, must refrain from directly or indirectly executing transactions in Philips shares and related rights. Additionally, employees have to comply with statutory rules and regulations concerning insider trading with respect to securities of other listed companies.

## 7. Business integrity

### 7.1 Bribery; records of transactions

Philips insists on honesty, integrity and fairness in all aspects of its business. Bribes in any form are unacceptable; commission payments and personal gifts or favors may only be made or accepted in strict accordance with the GBP Directives. Philips strives to comply with the highest levels of transparency and accountability throughout the company. Records of transactions should be maintained in an accurate, complete and timely manner in accordance with Philips accounting principles. No unrecorded funds or assets should be established or maintained.

### 7.2 Third-party interests

Employees are not allowed to have any direct or indirect financial interest in a supplier or competing company with the exception of a financial interest in a publicly traded company.

### 7.3 Political payments

Philips companies shall not make payments or donations, in money or in kind, to political parties, political organizations or individual politicians, unless such payments are made in strict accordance with the GBP Directives.

## 8. Observance of the General Business Principles

### 8.1 Sanctions

All Philips employees must comply with the General Business Principles. Violation may lead to disciplinary action, including dismissal, notwithstanding any further civil or criminal action that may be taken.

### 8.2 Whistleblower policy

In order to promote the reporting of violations of the General Business Principles, a whistleblower policy is in place, enabling employees to submit complaints on an anonymous basis without fear of the complaints leading to disciplinary action.

### 8.3 Compliance

Compliance with the General Business Principles is monitored via a worldwide network of Country and Product Division compliance officers, who regularly report to the Corporate Review Committee

GBP, which advises the Board of Management on the deployment of the General Business Principles and on ethical issues in general.

Reporting on compliance with the General Business Principles is also an integral part of the Statement on Business Controls issued annually by the management of each business unit/department as part of a cascade process leading to CEO/CFO certification of the company's annual accounts. Compliance processes and procedures are audited by Philips' Corporate Internal Audit department.

# Sustainability policy

*The Philips Sustainability Policy is a core element for the operations of the entire Philips organization. Sustainable development\* is a priority for the Board of Management, which has formulated guidelines for sustainable performance. This policy and resulting action programs are regularly reviewed and updated to meet stakeholder needs.*

## Philosophy

Since Philips was founded in 1891, it has worked to improve social equity and environmental quality, proving that responsible business is good business. Operating this way, the company has been able to improve economic prosperity for itself, its stakeholders and society at large. With its tradition of integrating economic, environmental and social issues, Philips understands that sustainable development is one of the most challenging issues facing the world.

## Commitment

Philips adheres to the Business Pledge for Action adopted by the world business community at the 2002 Johannesburg World Summit for Sustainable Development:

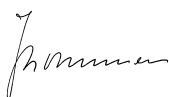
- Sustainability is the opportunity we embrace.
  - Responsibility is the standard by which we should expect to be judged.
  - Accountability is the obligation we assume.
  - Partnership is the pathway we pursue.
- Therefore, Philips will:
- Develop meaningful technology driven by the needs of society.
  - Behave responsibly, living up to the Philips values, brand promise and General Business Principles.
  - Continue to build and maintain trust through transparency and accountability.
  - Depend on and work with stakeholders inside and outside the company.

## Policy

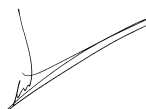
- Philips maintains and strengthens a culture of sustainable entrepreneurship, in line with its sustainability policy.
- Philips invests in its employees and creates a work environment that enables them to reach their full potential.
- Philips optimizes its innovations, business strategy and operations by setting financial and non-financial targets and maintaining constructive relationships with stakeholders.
- Philips expects its business partners to be committed to sustainable development.
- Philips is active in the community, supporting initiatives to improve people's lives, and is focusing on education and healthcare, particularly for the underprivileged.
- Philips measures and verifies its sustainability performance and publishes results annually.
- Philips engages governments, non-governmental organizations (NGOs) and companies to explore new businesses and emerging markets to improve quality of life.



Gerard Kleisterlee



Jan Hommen



Arthur van der Poel



Ad Huijser



Gottfried Dutine

\* Sustainability is defined as "meeting the needs of the present generation without compromising the ability of future generations to meet their own needs." Sustainable development – which is considered the path to sustainability – is the simultaneous pursuit of economic prosperity, environmental quality and social equity. Companies that pursue this path are known as sustainable entrepreneurs.



## EcoVision 2002-2005

# Environmental action program

### Product improvements

Philips product developers follow EcoDesign principles and focus on one or more of the following Green Focal Areas



Weight



Hazardous substances



Energy consumption



Packaging



Recycling and disposal

	Mandatory target	Recommended target
EcoDesign <sup>1</sup>	Level 6 on maturity grid	Level 8 on maturity grid
Green Flagship products <sup>2</sup>	One per product division per year	One per business per year
Packaging	Maintain performance	10% reduction
Supplier management <sup>1</sup>	Level 6 on maturity grid	Level 8 on maturity grid

### Process improvements

	Mandatory target	Recommended target
Energy	10%	20%
Waste	20%	30%
Water	15%	20%
Emissions to air and water		
Restricted substances (category I)	70%	90%
Hazardous substances (category II)	30%	50%
Environmentally relevant substances (category III)	15%	30%
Packaging	Maintain performance	10% reduction
Supplier management <sup>1</sup>	Level 6 on maturity grid	Level 8 on maturity grid
ISO 14001 certification	All manufacturing sites	All facilities

<sup>1</sup> Maturity grids range from 0-10, with 10 representing world class.  
N.B.: All targets are to be achieved by 2005 compared to reference year 2001, except where noted. Targets are relative and results incorporate correction for production fluctuations.

<sup>2</sup> A Green Flagship is defined as a product or product family that has gone through divisional EcoDesign procedures and, after investigation in three or more Green Focal Areas, has proven to offer better environmental performance in two or more of these areas, compared with its predecessors or closest commercial competitors.

# PHILIPS

# Occupational health and safety policy

## Philosophy

Since Philips was founded in 1891, it has worked to improve social equity and environmental quality, proving that responsible business is good business. Operating this way, the company has been able to improve economic prosperity for itself, its stakeholders and society at large. With its tradition of integrating economic, environmental and social issues, Philips understands that sustainable development is one of the most challenging issues facing the world.

## Commitment

Occupational Health and Safety, as an integral part of our doing business, must be incorporated into every action we undertake: there is no activity so important or urgent that cannot be done in an appropriate and safe way.

A persistent strive towards an injury and illness-free work environment is both a matter of responsibility and profitability: the quality of our activities and our success as a group are strongly determined by the maintenance of high standards at work, and primarily by consistent and continuing efforts on prevention of incidents and occupational disorders.

All individuals within Philips share this responsibility for achieving a world-class level in Occupational Health and Safety, as well as in quality of work and productivity: everyone is to be concerned about his/her person, fellow employees, public health and company property.

## Policy

Philips aims at maintaining a safe and healthy work environment for its employees, contract labour and visitors, and therefore is committed to do all that is reasonably feasible to:

- Meet or exceed requirements laid down in applicable Health and Safety laws and regulations, as well as voluntary standards to which Philips subscribes;
- Implement procedures for the identification, prevention and minimization of hazards and risks;
- Provide all employees with relevant information and regular training on Occupational Health and Safety aspects;
- Consult and co-operate with employees and/or their representatives;
- Maintain preventive practices and responsive procedures with regard to emergencies and accidental events;
- Be fully transparent in the periodical reporting on Health and Safety performance;
- Promote a Plan-Do-Check-Act approach at all levels in the organization in order to ensure continuous improvement.



# Social investment policy

## Philosophy

Since Philips was founded in 1891, it has worked to improve social equity and environmental quality, proving that responsible business is good business. Operating this way, the company has been able to improve economic prosperity for itself, its stakeholders and society at large. With its tradition of integrating economic, environmental and social issues, Philips understands that sustainable development is one of the most challenging issues facing the world.

## Commitment

Philips is active in the community, supporting initiatives to improve people's lives, and is focusing on education and healthcare, particularly for the underprivileged.

## Policy

- Philips makes optimal use of its own resources, both in terms of money and other assets, which may include:
  - Facilities (for instance by hosting meetings and events on company premises);
  - Products (for instance by donating and collecting products, including the redistribution of used products, or leasing equipment for organizations);
  - Technology (for instance by training on the use of equipment).
- Philips encourages its employees to use their skills and expertise as volunteers, in agreement with their management.
- Philips values working through partnerships with stakeholders like NGOs, local communities and/or officials.
- Philips carefully considers the value of being a key contributor, making a visible and unique difference with its own knowledge, expertise or products, rather than being just one of many supporters.
- Philips pursues balanced communications that illustrate the company's contribution to particular initiatives and their social impact, without being exploitative.

The Philips logo, consisting of the word "PHILIPS" in a bold, blue, sans-serif typeface.



## A selection of social investment projects 2004

Location	Project	Description
Australia	Starlight Foundation	Philips provides a range of electronic equipment, as well as other forms of entertainment, to seriously ill children and their families.
Austria	Philips Schülerfonds der Caritas	Philips financially assists educational activities and sponsors Future Vouchers to support schoolchildren from disadvantaged backgrounds after they leave statutory school. This program won the 2004 Austrian TRIGOS award for Corporate Social Responsibility.
Belarus	Boarding School	Company donations supported a Boarding School for orphans and children with limited abilities, providing Christmas presents, help in refurbishing the facility and computer training courses.
Belgium	E-solidarity	The E-Bridge program, sponsored by Philips, aims at bringing healthy and ill children together by exchanging experiences and communicating about healthy living and eating habits to create solidarity.
Brazil	Escola de Informatica e Cidadania	In partnership with a local non-governmental organization (NGO), Philips employees volunteer to lecture about informatics and citizenship. Sessions are hosted at Philips facilities in São Paulo, Mauá, Manaus and Recife.
Brazil	Se Liga, Moçada!	Philips employees work with youngsters, discussing issues including violence, relationships and job opportunities, as well as organize educational activities to provide basic professional skills.
Bulgaria	Trust in Life	Philips provides computer systems to three schools and scholarships in cooperation with the Bulgarian Ministry of Education.
Canada	Gilda's Club	Gilda's Club uses Philips donations to provide emotional, social and financial support to cancer patients and their families.
Canada USA	Habitat for Humanity	Philips supported Habitat for Humanity in its mission to end poverty housing in the US and around the world.
China	Project HOPE	Since 1998 Philips is an active supporter of Project HOPE, a program launched by a non-governmental, non-profit organization to help disadvantaged children resume their education. To enhance employee awareness of the project, donation drives were held on employee days in 2004.
Croatia	Pediatric wards	Philips refurbished and equipped pediatric wards in city hospitals.
France	Telethon	Philips and its employees support medical research to benefit people with rare diseases.
Germany	Anne Frank	Philips replaced the lighting in the Anne Frank Museum in Berlin.
Greece	Anichti Angalia Aglaia Kyriakou	Philips provided products including monitors, audio-visual equipment and a PC to an institution for children with chronic illnesses and to schools in the Grevena area.
India	Arogya Kiran	In association with the Trust for Reaching the Unreached, Philips Fellowships allow doctors to improve the quality of healthcare services in villages with inadequate facilities.
India	FIDES	Philips Software Center sponsors income-generation programs implemented by Family Integral Development Education Scheme (FIDES), a charitable voluntary organization benefiting disadvantaged families.
India	Philips brightlife studentship	With the help of SNS Foundation Gurgaon India, Philips facilitates access to education of children from disadvantaged families.
Indonesia	Football and Beyond	Financial support from Philips allows approximately 120 children from the Street Children Soccer team meet expenses for uniforms, shoes and other fees.
Ireland	St. Michael's House	Philips provides IT support and local training to develop an intranet site for St. Michael's House, which provides online access to specialized educational and training programs to adults and children with learning disabilities.
Italy	Il cuore a scuola	This Philips research program on cardiac diseases at an early age provides screening and education for school children.
Mexico	Healthcare services	Philips provides free healthcare services to employees, their families and the neighboring community, including immunization programs, breast cancer screening and blood tests.
Netherlands	Leergeld Foundation	Philips' financial aid and management expertise help the Leergeld Foundation prevent social exclusion of children from lower income families. Financial assistance allows children to participate in such social activities as sports and youth clubs.
Netherlands	Zonnetjes in huis	Philips Lighting in Weert partners with a center for mentally challenged people, offering small groups the opportunity to perform light manual activities (like packaging) in the Lighting factory.
New Zealand	Cure Kids	Philips supports the Child Health Research Foundation with donations, fundraising and other activities.
Philippines	Relief for Real	Philips Cabuyao arranged donations, canned goods and clothing for the village of Real (Quezon), stricken by a flood. Employees distributed these relief goods.
Portugal	Acreditar	Philips donations are used to maintain apartments in Lisbon for childhood cancer patients and their families who travel a distance for treatments.
Russia	Speransky Children Hospital	Philips supports the Surgery and Burn Wings for children undergoing a long-term course of treatment.
South Africa	SOAR	Through the SOAR program (Supply Opportunity and Achieve Results), each Philips division adopts a school and organizes educational activities for the pupils.
Spain	Asion	Thanks to Philips, a special hospital space was created for children affected by cancer.
Turkey	Computer education on the move	Philips sponsors two mobile education units operated by the Turkish Education Volunteer Foundation, which provides basic computer knowledge to children ages 7-14.
UK	The Mother and Baby	Philips supports this charity, which provides healthcare for mothers, providing donations, free lectures, training and discounted equipment.
USA	American Heart Association	Philips supports the American Heart Association and sponsors its Annual Heart Walks. Hundreds of employees and their families volunteer to participate in the event.

## Maturity Grid, EcoDesign in Product Creation Process (version 2.0)

- 0 The development department delivers products without attention to their environmental consequences; no programs or tools exist to address this issue.

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- 1 Environmental issues are taken into account only incidentally and mainly driven by individual initiatives. Environmental risks to the business are not identified or assessed. There are first signs of methods and tools; remedial features are introduced to correct unwanted environmental effects.

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- 2 An EcoDesign procedure including mandatory environmental requirements is available in a development center. A development center's Product Creation Process (PCP) refers to this EcoDesign procedure.

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- 3 The available EcoDesign procedure covers all elements of the 'framework for EcoDesign Procedures'. This EcoDesign procedure is used in some projects. A management system (like ISO 14001/9001/other) is in place in a development center.

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- 4 The EcoDesign procedure is used in many projects. The EcoDesign procedure is integrated in the management system (like ISO 14001/9001/other). Environmental roadmaps (or environmental targets/ improvement trends in technology roadmaps authorized by management of a development center) are available in a development center.

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- 5 A mandatory EcoDesign procedure is in place in a development center. The EcoDesign procedure is used in most projects. An annual internal auditing process covers the EcoDesign procedure. This Maturity grid is off-line included as extra element in the Process Survey Tool 'PCP' of a development center.

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- 6 The EcoDesign procedure is used in all projects. Environmental roadmaps are used as input for target setting in the EcoDesign procedure. Environmental roadmaps are updated annually. This update process is integrated in the management system (like ISO 14001/9001/other). The Maturity Grid 'EcoDesign in PCP' is included as extra element in the Process Survey Tool 'PCP' of a development center. The reached level of Maturity Grid element 'EcoDesign in PCP' is part of annual Business Review.

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- 7 A development center's management system (like ISO 14001/9001) is certified externally. Targets/ improvement trends in environmental roadmaps are based on environmental performance benchmarks with competitor or predecessor products/technologies.

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- 8 An annual external auditing process covers the EcoDesign procedure. Several objectives in environmental roadmaps are set to surpass environmental performance of competitor products. Development projects are started to reach those objectives. The grid level is reported in BEST Society Results 8b.

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- 9 The position in the top 5 among competitors is confirmed by external reports, activities or prizes obtained for many key products that excel on environmental performance. The organization knows what steps have to be taken to reach the top position among competitors. Plans are ready and in place to reach that position.

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- 10 Recognition by competitors and others for best practices. Self learning organization focused on sustained business excellence, fully integrated with partners.

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## Green Flagships benchmark details

	Unit	Competitor A	Competitor B	Competitor C	Predecessor	Average	Philips Green Flagship	Improvement %
<b>M3176C USB 2-Channel Recorder</b>								
Energy	[kWh/year]				124		114	8
Weight	[Kg]				2.56		1.56	39
Packaging	[lbs]				1.18		0.84	29
Recycling and disposal	[%recyclable materials]				38		50	12
<b>MML1921 monitor</b>								
Weight	[Kg]				11.4		10.32	9
Packaging	[Kg]				4.11		2.68	35
<b>IU 22 Ultrasound system</b>								
Weight	[lbs]				442		344	22
Hazardous substances	[mg Hg]				14		2.5	82
Energy	[kWh/year]				4569		2886	37
Recycling and disposal	[%recyclable materials]				41		71	30
Packaging	[lbs]				50		40	20
<b>190S5 LCD monitor</b>								
Energy	[kWh/year]	62	66	71		66.3	51	23
Packaging	[g]	1239	1569	1431		1413	786	44
Packaging	[products/container]	1150	1012	960		1041	2030	95
<b>Xenium 9@9c mobile phone</b>								
Weight	[g]	320	300			310	244	21
Energy	[kWh/year]	1.6	4.7			3.2	1.2	62
<b>KEY013 MP3 digital audio player</b>								
Weight	[g]	113	101	47		87	53	39
Energy	[kWh/year]	1.83	1	1.1		1.31	0.17	87
Packaging	[g]	179	235	237		217	115	47
Packaging	[products/container]	37674	20056	18224		25318	55695	120
<b>KEY015 MP3 digital audio player</b>								
Weight	[g]	116	48			82	52	37
Energy	[kWh/year]	1.67	1.03			1.35	0.07	95
Packaging	[g]							
Packaging	[products/container]	37128	27048			32088	55695	74
<b>MCV250 CD cassette player</b>								
Energy	[kWh/year]	85	42			64	27	57
Packaging	[g]	10456	9050			9753	6711	31
Packaging	[products/container]	973	960			967	1302	35
<b>DVD520 DVD player</b>								
Energy	[kWh/year]	27	18	16		20.3	10	51
Packaging	[g]	626	476	778		626.7	547	13
Packaging	[products/container]	3184	2864	2500		2849	4340	52
<b>32PF9956 Flat TV</b>								
Energy	[kWh/year]	251	305			278	131	53
Packaging	[g]	4209	5738			4974	3752	25
Packaging	[products/container]	162	180			384	171	55
<b>29PT7333 CRT TV</b>								
Energy	[kWh/year]	265	282			274	210	23
Packaging	[g]	5180	4938			5059	4689	7
Packaging	[products/container]	135	156			146	188	29

	Unit	Competitor A	Competitor B	Competitor C	Predecessor	Average	Philips Green Flagship	Improvement %
<b>TLD 30/840 Click-2-save</b>								
Energy	[lm/W]				79		93	18
Hazardous substances	[mg Hg]				8		3	63
Lifetime	[h]				13000		15000	15
<b>Cosmopolis Gold 6600 lumen</b>								
Energy	[lm/W]				75		97	29
Hazardous substances	[mg Pb]				1		0	100
Weight	[g]				51		32	37
<b>Cosmopolis White 6600 lumen</b>								
Energy	[lm/W]				73		105	44
Hazardous substances	[mg Hg]				4		1	75
Hazardous substances	[mg TI]				0.7		0.1	86
Weight	[g]				47		32	32
<b>Alto 25W T8</b>								
Energy	[lm/W]	97			78	88	96	11
Hazardous substances	[mg Hg]	7			4.7	5.9	3.5	40
Lifetime	[h]	26000			20000	23000	30000	30
<b>Master TL-D Extra</b>								
Hazardous substances	[mg Hg]	13.9	7.3			10.6	5	53
Packaging	[g]	31.2				31.2	24.2	22
Lifetime	[h]	18000	12000			15000	21000	40
<b>Master TL-D Extreme</b>								
Hazardous substances	[mg Hg]	13.9	8			11.0	5	54
Packaging	[g]	31.2				31.2	24.2	22
Lifetime	[h]	18000	36000			27000	36000	33
<b>Master QL 85W</b>								
Energy	[lm/W]	60					72	20
Lifetime	[h]	80000				80000	100000	25
<b>Master Colour Elite TC 35W</b>								
Energy	[lm/W]	51	71			61.0	95	56
Hazardous substances	[mg Hg]	3.1	2.7			2.9	2.5	14
Lifetime	[h]	3000	4000			3500	8000	129
<b>Azur Iron</b>								
Weight	[g]	1760	1660	1600		1673	1590	5
Packaging	[formula*]	1.49	0.69	0.99		1.06	0.43	59
<b>PCA2002U/10</b>								
Weight	[g]				19		1	95
Hazardous substances	[mg Pb]				0.2		0	100
Energy	[µW]				0.26		0.14	46
Packaging [342.000 pieces]	[kg]				9.863		1.046	89

\* Packaging formula =  $\frac{\text{Packaging weight}}{\text{product weight}} \times \frac{\text{box volume}}{\text{product volume}} \times \text{number of materials}$

## EcoVision data tables

## EMS: percentage of ISO 14001 certified reporting organizations

	2000	2001	2002	2003	2004
Lighting	95	91	92	93	99
Medical Systems	63	100	57	73	68
DAP	100	88	88	88	88
Consumer Electronics	83	91	91	100	80
Semiconductors	100	86	80	95	96
Components	80				
Other activities	79	80	87	82	96
Total	85	90	87	90	92

CO<sub>2</sub> emissions (tons)

	2000	2001	2002	2003	2004
Lighting	978,027	285,102	265,661	256,233	261,205
Medical Systems	27,169	10,796	11,672	12,253	10,545
DAP	54,562	5,276	5,236	5,866	5,659
Consumer Electronics	164,176	10,739	12,507	9,088	5,723
Semiconductors	673,204	53,040	50,361	50,275	49,317
Components	1,031,635				
Other activities	55,043	5,775	7,046	6,774	6,479
Total	2,983,816	370,728	352,483	340,489	338,928

## Packaging (tons)

	2000	2001	2002	2003	2004
Lighting	96,712	107,648	98,479	83,458	91,040
Medical Systems	2,255	3,924	4,392	5,182	4,798
DAP	22,517	16,248	19,470	16,931	16,161
Consumer Electronics	68,603	83,156	103,390	101,071	107,168
Semiconductors	6,818	6,583	6,364	7,014	7,446
Components	37,975				
Other activities	1,550	1,899	2,425	1,974	2,155
Total	236,430	219,458	234,520	215,630	228,768

## Total waste (tons)

	2000	2001	2002	2003	2004
Lighting	109,333	90,790	83,925	85,655	84,103
Medical Systems	2,708	5,781	6,738	7,449	7,388
DAP	5,100	7,761	8,269	8,818	7,906
Consumer Electronics	45,251	24,432	26,207	23,753	24,220
Semiconductors	22,853	19,156	18,345	20,393	20,283
Components	98,751				
Other activities	9,628	6,826	6,668	5,879	5,793
Total	293,624	154,746	150,152	151,947	149,693

## Energy consumption (PJ)

	2000	2001	2002	2003	2004
Lighting	15.5	12.4	11.9	11.6	12.2
Medical Systems	0.4	1.4	1.5	1.5	1.5
DAP	0.8	0.9	0.9	1.0	0.9
Consumer Electronics	2.5	0.7	0.6	0.7	0.7
Semiconductors	10.5	11.4	11.6	11.7	12.1
Components	16.0				
Other activities	0.9	0.9	1.0	1.0	1.0
Total	46.6	27.7	27.5	27.5	28.4

Water intake (10<sup>3</sup> m<sup>3</sup>)

	2000	2001	2002	2003	2004
Lighting	6,735	4,439	3,923	3,405	3,328
Medical Systems	204	441	485	466	475
DAP	434	404	422	424	443
Consumer Electronics	1,195	486	536	582	593
Semiconductors	10,666	10,251	10,019	9,722	9,974
Components	13,954				
Other activities	881	666	490	550	508
Total	34,069	16,687	15,875	15,149	15,321



#### Emissions from restricted substances (tons)

	2000	2001	2002	2003	2004
Lighting	13.4	7.9	5.3	2.9	1.6
Medical Systems	2.0	1.8	2.0	2.3	1.6
DAP	0.2	0.2	0.0	0.0	0.0
Consumer Electronics	0.0	0.0	0.0	0.0	0.0
Semiconductors	32.2	74.7	66.3	40.4	13.6
Components	2.0				
Other activities	12.0	2.1	1.5	0.0	0.0
<b>Total</b>	<b>61.8</b>	<b>86.7</b>	<b>75.1</b>	<b>45.6</b>	<b>16.8</b>

#### Emissions for hazardous substances (tons)

	2000	2001	2002	2003	2004
Lighting	45.7	88.0	46.4	16.4	11.4
Medical Systems	0.9	0.9	0.5	0.4	0.5
DAP	3.1	2.9	3.4	3.1	1.9
Consumer Electronics	22.4	0.0	0.0	0.0	0.0
Semiconductors	64.4	86.0	75.7	82.0	80.6
Components	454.0				
Other activities	6.9	15.5	13.8	10.6	11.9
<b>Total</b>	<b>597.4</b>	<b>193.3</b>	<b>139.8</b>	<b>112.5</b>	<b>106.3</b>

#### Emissions for relevant substances (tons)

	2000	2001	2002	2003	2004
Lighting	3,631	3,932	4,015	3,367	3,340
Medical Systems	11	45	57	62	57
DAP	92	114	139	106	68
Consumer Electronics	1,405	528	866	243	74
Semiconductors	2,563	2,671	2,643	2,419	2,506
Components	2,746				
Other activities	93	66	70	68	76
<b>Total</b>	<b>10,541</b>	<b>7,356</b>	<b>7,790</b>	<b>6,265</b>	<b>6,121</b>

# PHILIPS

Date: 10/12/2003  
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## Supplier Declaration on Sustainability

Supplier : \_\_\_\_\_

### General

Supplier is committed to act fairly and with integrity towards stakeholders and is expected to comply with all applicable local rules and regulations.

### Environment

Supplier shall have ISO14001 certification or a plan to become certified. Alternatively supplier must provide documented objective evidence of an operational environmental management system for ISO14001 or demonstrate equivalency which shows continual environmental improvement. Suppliers must comply with requirements of the respective Product Division, including banned/hazardous substances content.

### Health and safety

Supplier shall do all that is reasonable and practicable to:

- Protect the health and safety of employees and contract labour and minimize any adverse work conditions;
- Implement safe and healthful workpractices to prevent injury, illness and property damage;
- Minimize occupational exposures to potentially hazardous materials and unsafe work conditions by maintaining appropriate safety systems and effective controls;
- Implement an emergency response program that addresses the most likely anticipated emergencies;

- Train managers and employees to assure their continued commitment to their own health and safety and that of their co-workers;
- Involve employees at all levels in the health and safety program; assure their accountability for injury and illness prevention.

### Child labour

Supplier shall not employ children in violation of convention 138 and 182 of the International Labour Organization. In case of child labour, Supplier shall take immediate remedial action in consultation with Philips, considering the interests of the children employed. This action will include:

- Minimally acceptable employment conditions for the children employed (such as education, working hours, wages, medical facilities etc.);
- The obligation of the supplier not to employ any more children;
- A time period within which the supplier will comply with the mentioned ILO norms.

### Forced labour

Employment should be freely chosen. Under no circumstances will Supplier make use of forced or bonded labor – such as forced labor performed by persons placed in an institution, or compulsory labor including labor as a means of political coercion or education – to design, manufacture or assemble products and services for Philips.



## Right to organize

Supplier shall recognize and respect the freedom of its employees to choose whether or not to establish or to associate with any organization of their own choosing (including labor unions) without Suppliers' prior authorization. The employment of a worker shall not be contingent upon the condition that he/she not join a union or be forced to relinquish trade union membership. Furthermore, union membership shall not be the cause for the dismissal of – or otherwise prejudice against – a worker. Supplier will not interfere with or finance labor organizations or take other actions with the intent of placing such organization under the control of Supplier.

## Collective bargaining

Supplier shall respect – within the framework of law, regulations and prevailing labor relations

and employment practices – the right of its employees to be represented by labor unions and other employee organizations. Supplier will engage in negotiations, either on its own behalf or through employers' associations, with a view toward reaching agreement on employment conditions.

## Discrimination

Supplier shall treat its employees equally in employment and occupation, and will ensure that each has equal opportunities. Supplier shall offer equal pay for equal work performed at equal levels. No form of harassment or discrimination in respect of employment and occupation will be tolerated, such as discrimination based on race, color, sex, age, language, religion, political or other opinion, national or social origin, property, birth or other status.

Declaration to be signed by Supplier:

Name: \_\_\_\_\_ ( Company Stamp)

Function: \_\_\_\_\_

Date: \_\_\_\_\_

Signature: \_\_\_\_\_



## Royal Philips Electronics List of Banned Substances (CSO-BP01-2004-1)

Revision date: 2004-07-15

Articles (i.e. materials, components, subassemblies, products) delivered to Royal Philips must be free of the "Banned substances" as mentioned in this list.

Substances	Declaration threshold ppm (mg/kg) <sup>1</sup>	Legal date entry into force
Cadmium and –compounds	20	Immediately
Mercury and –compounds	2	Immediately
Lead and – compounds	1000	1 July 2006
Lead and – compounds in outer sleeves of cables, according to proposition 65 legislation, USA	300	Immediately
Hexavalent Chromium (Cr 6+) and compounds	1000	1 July 2006
Asbestos (all types)	10	Immediately
CFCs, Chlorofluorocarbons	1	Immediately
HCFCs, Hydrogenated chlorofluorocarbons	1	Immediately
Halons	1	Immediately
CHCs, Chlorinated hydrocarbons,	1	Immediately
Methyl Bromide	1	Immediately
HBFCs, Hydrobromofluorocarbons	1	Immediately
1,1,1-Trichloroethane	1	Immediately
Carbon tetrachloride	1	Immediately
Dichloromethane (CH <sub>2</sub> Cl <sub>2</sub> )	1	Immediately
Trichloroethylene (C <sub>2</sub> HCl <sub>3</sub> )	1	Immediately
Perchloroethylene (C <sub>2</sub> Cl <sub>4</sub> )	1	Immediately
PCBs, polychlorinated biphenyls	10	Immediately
PCTs, polychlorinated terphenyls	10	Immediately
PCP, Pentachlorophenol and its salts and esters	10	Immediately
Polybrominated diphenyl ethers (PBDEs)	1000	Immediately
Polybrominated biphenyls (PBBs)	1000	Immediately
Ugilec 141 (monomethyl tetrachlorodiphenyl methane)	10	Immediately
Ugilec 121 (or Ugilec 21) (monomethyl dichlorodiphenyl methane)	10	Immediately
DBBT (monomethyl dibromodiphenyl methane)	10	Immediately

Product packaging must be free from the above-mentioned substances AND the following:

Substances	Declaration threshold ppm (mg/kg) <sup>1</sup>	Legal date entry into force
PVC and PVC blends	1000	Immediately
Sum of Heavy metals (Cd, Hg, Cr(6+) and Pb)	100	Immediately

Note:

For Product Division (PD) additional banned substances and specific exemptions on above list, see appendix to this Royal Philips Electronics list of Banned Substances.

## Appendix in addition to Royal Philips Electronics list of Banned Substances CSO-BP01-2004-1

Additional Banned Substances and specific exemption per Product Division (PD)

### Philips Consumer Electronics (CE)

Additional Substance(s) and different legal dates	Declaration threshold ppm (mg/kg)	Entry into force	Remark
Short-chain chlorinated paraffins	10	Immediately	(C10-C13) used in paints and as flame retardant in PVC
Organostannic compounds	10	Immediately	Organic Tin compounds (TBT, TPT and TBTO compounds)
TBBA (tetrabromobisphenol-A)	10	1 Jan 2006	Applied as FR in Laminates of printed wiring boards (PWBs) also in plastics
Azocolourants	30	Immediately	Applied in leather and textiles in prolonged skin contact
Nickel and nickel alloys	0,5µg/cm2/week	Immediately	Only in prolonged skin contact,
Tris-(1-aziridinyl) phosphin oxide	10	Immediately	Applied in leather and textiles in prolonged skin contact
Tris-(2,3-dibromo-propyl) phosphate	10	Immediately	Applied in leather and textiles in prolonged skin contact
Lead and - compounds	1000	1 Jan 2005	This is before the legal date (EU Directive RoHS 2002/95/EC)
Hexavalent Chromium (Cr 6+) and compounds	1000	1 Jan 2005	This is before the legal date (EU Directive RoHS 2002/95/EC)

CE Requirements to phenol in laminates of printed wiring boards:

1. Smell Emission : <200 odor unit/m2/day  
Test method: Measured in duplo according to NVN2820 (or NEN-EN 13725:2003) by TNO Apeldoorn, the Netherlands, with 10 dm2 of single sided copper clad laminate after 3 days at room temperature in a PTFE bag of approximately 40 l.
2. Phenol monomer : <50 mg/l phenolics  
Test method : Phenolics content in water (according to ISO 6439) after shaking for 23 hours a mixture of 75 g of milled (to 3 mm) laminate in 1.5 l of demineralized water at pH 4).

### Philips Domestic Appliance and Personal Care (DAP)

Additional Substance(s) and different legal dates	Declaration threshold ppm (mg/kg)	Entry into force	Remark
EPS (Expanded Polystyrene)	1000	Immediately	Banned for Product Packaging (with a product weight of less than 20 kg)

Exemption information:

DAP is re-enforcing its limit for the cadmium-threshold from 100 ppm to 20 ppm. Final entry into force of this new more stringent value is January 1st, 2006.

### Philips Lighting

Additional Substance(s) and different legal dates	Declaration threshold ppm (mg/kg)	Entry into force	Remark
Antimony in soda lime glass	1000	Immediately	The antimony is present as an impurity, not intentionally added to the glass.
Polycyclic aromatic hydrocarbons (PAHs)	5	Immediately	All applications. (like potting material for electronic ballast)
TBBA (tetrabromobisphenol-A)	10	1 Jan 2006	Applied as FR in Laminates of printed wiring boards (PWBs) also in plastics.

Exemption information:

Mercury is allowed only in gas discharge lamps with certain conditions referred in European Directive RoHS 2002/95/EC. This restriction applies only for lamps placed on the European market since 1st July, 2006.



### Philips Medical Systems (PMS)

Additional Substance(s) and different legal dates	Declaration threshold ppm (mg/kg)	Entry into force	Remark
Arsenic compounds	10	Immediately	Banned for wood Packaging

Exemption information:

Lead and compounds, and Hexavalent Chromium (Cr 6+) and compounds are only mentioned in the new European Directive RoHS 2002/95/EC and not in any other legislation. Presently Medical equipment is exempt from this RoHS Directive. Therefore these substances are not Banned for PMS and no Request for Dispensation is required.

This exemption does not include Lead in outer sleeves of cables in accordance with proposition 65 .

### Philips Semiconductors

Additional Substance(s) and different legal dates	Declaration threshold ppm (mg/kg)	Entry into force	Remark
Short-chain chlorinated paraffins	10	Immediately	(C10-C13) used in paints and as flame retardant in PVC
Organostannic compounds	10	Immediately	Organic Tin compounds (TBT, TPT and TBTO compounds)
Polychloronapthalenes	10	Immediately	> 3 Cl atoms as stabilizer and flame retardant in plastics
Benzene	100	Immediately	As residual solvent in materials
Formaldehyde	0.1	Immediately	As residue in plastics, resins
Lead and - compounds	1000	1 Jan 2005	This is before the legal date (EU Directive RoHS 2002/95/EC)
Hexavalent Chromium (Cr 6+) and compounds	1000	1 Jan 2005	This is before the legal date (EU Directive RoHS 2002/95/EC)

## List of substances\*

### List of Category I substances

- Asbestos (all types)
- Benzene
- Beryllium and compounds (Be)
- Cadmium and compounds (Cd)
- DBBT (monomethyl-dibromo-biphenylmethane)
- Dibenzofurans
- Dioxins
- Halogenated hydrocarbons, like CHCs, CFCs, HCFCs according to the UD-D 1787 standard
- Mercury and compounds (Hg)
- Polybrominated biphenyl ethers (PBBEs)
- Polybrominated biphenyls (PBBs)
- Polycyclic aromatic hydrocarbons
- Polychlorinated biphenyls (PCBs) & Polychlorinated terphenyls (PCTs)
- Polyvinylchloride (PVC and PVC blends in packaging materials for consumer end products)
- Radioactive substances
- Ugilec 121 (or Ugilec 21: monomethyl-dichloro-biphenylmethane)
- Ugilec 141 (monomethyl-tetrachloro-biphenylmethane)
- Vinylchloride (monomer)

### List of Category II substances

- Acrylonitrile (monomer)
- Antimony and compounds (Sb)
- Arsenic and compounds (As)
- Azo dyes
- Chromium(VI) compounds (Cr-VI)
- Cobalt and compounds (Co)
- Cyanides
- Diethylamine & dimethylamine
- Epichlorohydrine (monomer)
- Formaldehyde (monomer)
- Halogenated organic compounds (other than mentioned in Category I restricted substances)
- Hydrazine
- Lead and compounds (Pb)
- Metal carbonyls
- 2-methoxy or 2-ethoxy-ethanol, and 2-methoxy- or 2-ethoxy-ethyl acetate
- N,N-dimethylacetamide (DMA) & N,N-dimethylformamide (DMF)
- Nitrosamide & Nitrosamine
- N-methylacetamide (NMA) & N-methylformamide (NMF)
- Organic tin compounds (Sn)
- Pentachlorophenol & Phenol (monomer)
- Per Fluorinated Compounds, PFCs
- Phthalates (all)
- Picric acid
- Selenium and compounds (Se)
- Tellurium and compounds (Te) & Thallium and compounds (Tl)
- Toluene
- Xylenes

### List of Category III substances

- Boron and -compounds (B)
- Hydrofluoric acid (HF)
- Hydrochloric acid
- Nitrates
- Nitric acid & sulphuric acid
- Nitrogen oxides (power stations/boilers)
- Nitrogen oxides (processes)
- Phosphates
- Phosphoric acid
- Rare earth metals (lanthanum and heavier)
- Sulphur oxides (processes)
- Transition 'heavy' metals (e.g. Ag, Ba, Cr, Cu, In, Mo, Ni, Pd, Sn, Ti, V, W, and Zn)
- VOCs (=Volatile Organic Compounds, like acetone, cyclo-hexanone, isopropyl alcohol, methanol, methyllethylketone, and styrene)

\* in production

## Global Reporting Initiative (GRI) Guidelines – General

	Indicator number		Page/s	Remark
<b>Vision and strategy</b>				
	1.1	Statement of the organization's vision and strategy regarding sustainable development	16-35	
	1.2	Statement from the CEO describing key elements of the report	4-7	
<b>Profile</b>				
Organizational profile	2.1	Name of reporting organization	cover	
	2.2	Major products and/or services, including brands if appropriate	9-10	
	2.3	Operational structure of the organization	9	
	2.4	Description of major divisions, operating companies, subsidiaries and joint ventures	9-10	
	2.5	Countries in which the organization's operations are located	9	
	2.6	Nature of ownership; legal form	10	
	2.7	Nature of markets served	10, 38	
	2.8	Scale of the reporting organization	2, 9-10	
	2.9	List of stakeholders, key attributes of each, and relationship to the reporting organization	20-21	
Report scope	2.10	Contact person(s) for the report, including e-mail and web addresses	112	
	2.11	Reporting period	cover, 2	
	2.12	Date of previous report	20	
	2.13	Boundaries of report (countries/regions, products/ services, etc.) and any specific limitations	2, 86-87	
	2.14	Significant changes in size, structure, ownership	9-10	
	2.15	Basis for reporting on joint ventures etc. affecting comparability from period to period	2, 18	
	2.16	Explanation/nature of any re-statements of earlier reports (e.g. mergers/acquisitions)	86-87	
Report profile	2.17	Decisions not to apply GRI principles/protocols in the preparation of the report		in this column
	2.18	Criteria/definitions used in accounting for cost/benefits	73-79	
	2.19	Significant changes in measurement methods	86-87	
	2.20	Policy and internal practices to enhance accuracy, completeness and reliability	84, 86-87	
	2.21	Policy and current practice on independent assurance	84	
	2.22	Means by which report users can obtain additional information	112	

	Indicator number		Page/s	Remark
<b>Governance structure and management systems</b>				
Structure and governance	3.1	Governance structure of the organization (incl. major committees)	10-15	
	3.2	Percentage of the Board of Directors (Supervisory Board) that are independent/non-executive directors	10	
	3.3	Process for determining the expertise board members need to guide strategic direction		Not inventorized
	3.4	Board-level processes for overseeing economic/environmental/social risks and opportunities	13, 16-19	
	3.5	Linkages between executive compensation and achievement of non-financial goals		Not inventorized
	3.6	Organizational structure/responsibilities for oversight, implementation and audit of relevant policies	10-15	
	3.7	Mission/values/codes of conduct/principles and status of implementation	13-15, 24	
	3.8	Mechanisms for shareholders to provide recommendations to Board of Management	11	
Stakeholder engagement	3.9	Basis for identification and selection of major stakeholders	20-21	
	3.10	Approaches to stakeholder consultation in terms of frequency of consultations by type	20-23, 38, 44-47, 80-82	
	3.11	Type of information generated by stakeholder consultations	13, 20-23, 25, 38-39, 44-47, 81-82	
	3.12	Use of information resulting from stakeholder engagements	13, 20-23, 38-39, 44-47, 81-82	
Overarching policies and management systems	3.13	Explanation of how the precautionary principle is addressed by the organization's policies	57, 90, 92	
	3.14	Subscription to externally developed/voluntary charters/principles/initiatives	2, 11-13, 51	
	3.15	Principal industry and business association membership	17	
	3.16	Policies/systems for supply chain management and product stewardship	59-66, 80-82, 102-104	
	3.17	Approach to managing indirect impacts resulting from activities	58-67	
	3.18	Major decisions regarding locations or changes of operations	42-45	
	3.19	Programs and procedures for improvement programs/actions	18-21, 45-51, 60-70, 91, 95	
	3.20	Status of certification of environmental, labor, social accountability management systems	51, 66	

## Global Reporting Initiative (GRI) Guidelines – Core Indicators

	Indicator number		Page/s	Remark
<b>Economic performance indicators</b>				
Customers	EC1	Net sales	9, 74	
	EC2	Geographic breakdown of key markets	74-75	
Suppliers	EC3	Cost of all goods, materials and services purchased	80	Under investigation
	EC4	Percentage of contracts paid in accordance with agreed terms		
Employees	EC5	Total payroll and benefits broken down by country/region	75	
Providers of capital	EC6	Distribution to providers of capital broken down by interest/dividends on all classes of shares	78	
	EC7	Increase/decrease in retained earnings (ROACE)		Not inventorized
Public sector	EC8	Total sum of taxes per geographic region		Not inventorized
	EC9	Subsidies received per geographic region		Not inventorized
	EC10	Donations to community/civil society, broken down in terms of cash/in-kind	52-55, 94	
<b>Environmental performance indicators</b>				
Materials	EN1	Total materials use, other than fuel and water, by type		Not inventorized
	EN2	Percentage of materials used that are waste from sources external to the reporting organization		Not inventorized
Energy	EN3	Direct energy use segmented by primary source	58, 66-67, 98	
	EN4	Indirect energy use	58	
Water	EN5	Total water use	68-69, 98	
Biodiversity	EN6	Location and size of land owned, leased or managed in biodiversity-rich habitats		Not applicable
	EN7	Description of the major impacts on biodiversity in terrestrial, freshwater and marine environments		Not applicable
Emissions, effluents and waste	EN8	Greenhouse gas emissions	58, 67, 98	
	EN9	Use and emissions of ozone-depleting substances	69, 99, 105	
	EN10	NO <sub>x</sub> , SO <sub>x</sub> and other significant air emissions by type	69-70, 99, 105	
	EN11	Total amount of waste by type and destination	68, 98	
	EN12	Significant discharges to water by type	69-70	
	EN13	Significant spills of chemicals/oils/fuels in terms of total number and total volume	70	
Products and services	EN14	Significant environmental impact of principal products and services	62-65, 96-97	Not aggregated
	EN15	Percentage of weight of products sold reclaimable/reclaimed after use		Not inventorized
Compliance	EN16	Incidents of and fines for non-compliance associated with environmental issues	70	

	Indicator number		Page/s	Remark
<b>Social performance indicators Labor practices and decent work</b>				
Employment	LA1	Geographical breakdown of workforce, where possible by region/country/status	42-43	
	LA2	Net employment creation and average turnover segmented per region/country	43	
Labor/Management Relations	LA3	Percentage of employees represented by independent trade union per region/country		Not inventorized
	LA4	Policy and procedure on information, consultation with employees (e.g., restructuring)	44-45	
Health & Safety	LA5	Practices on recording/notification of occupational accidents/diseases (relation to ILO)	48-51	
	LA6	Description of formal joint H&S committees/ proportion of workforce represented in committees		Not inventorized
	LA7	Standard injury, lost day and absent rates and work-related fatalities	48-51	
	LA8	Description of policies or programs (for the workplace and beyond) on HIV/AIDS	50, 54	
Training & Education	LA9	Average hours of training per year per category of employee		Not inventorized
Diversity and opportunity	LA10	Description of equal opportunities policies or programs	46-48	
	LA11	Composition of senior management and corporate governance bodies (including board of directors)	10, 46	
<b>Human rights</b>				
Strategy and management	HR1	Description of policies, corporate structure on human rights and monitoring mechanism and results	14, 51	
	HR2	Evidence of consideration of human rights (investment/procurement/suppliers/contractors)	80-83	
	HR3	Description of policy on human rights for supply chain and contractors; monitoring systems/results	80-83, 100-101	
Non-discrimination	HR4	Description of global policies preventing all forms of discrimination and monitoring systems/results	13-15, 51, 88	
Freedom of association/ collective bargaining	HR5	Description of policies on freedom of association and programs	51, 88	
Child Labour	HR6	Description of policy excluding child labor, monitoring systems and results	15, 51, 88	
Forced and compulsory labor	HR7	Description of policies on forced and compulsory labor, monitoring systems and results	51, 88	
<b>Society</b>				
Community	SO1	Description of policy on community impact, programs and monitoring systems and results	52-55, 93, 94	
Bribery and corruption	SO2	Description of policy on bribery and corruption, and compliance mechanisms	14, 89	
Political contributions	SO3	Description of policy for managing political and lobbying contributions, and compliance mechanisms	14, 89	
<b>Product responsibility</b>				
Customer health and safety	PR1	Description of policy on customer health and safety through products and services, and results	40-41	
Products and services	PR2	Description of policy on product information and labeling, and compliance mechanisms	40-41	
Respect for privacy	PR3	Description of policy and management system for consumer privacy, and compliance mechanisms	39-40	





## Glossary

BEST	Philips business excellence model 'Business Excellence through Speed and Teamwork'
CFC	Chlorofluorocarbon CFCs are considered deleterious to the ozone layer.
CHC	Chlorohydrocarbon
CO <sub>2</sub>	Carbon dioxide This is the most prevalent greenhouse gas.
Eco-Indicator	Life Cycle Analysis-oriented tool which expresses environmental impact in a one-figure score (points, millipoints)
Environmental Management System	That part of an organization's general management system which includes organizational structure, responsibilities, planning activities, method development, work practices, processes and resources for developing, implementing, evaluating and maintaining the organization's environmental policies. An environmental management system makes it possible to formulate clear goals for environmental work, systematic follow-up of results and documentation of practices and activities.
FTE	Full-time equivalent
GJ	Gigajoule The Joule (J) is the basic energy unit of the International System of Units (SI). It is ultimately defined in terms of the meter, kilogram and second. Giga is the metric prefix indicating 10 <sup>9</sup> times base unit (1 followed by 9 zeroes).
Global warming	The increasing temperature of the atmosphere due principally to the burning of fossil fuels like coal, gas and oil in power stations and vehicles.
HCFC	Chlorofluorocarbon with one or more hydrogen atoms HCFCs are an alternative to CFCs, with approximately one tenth of their ozone-depleting properties and greenhouse effect.
ILO	International Labour Organization
ISO 14001	International standard that forms the basis for setting up, auditing and certifying environmental management systems. It has been formulated by the International Standardization Organization (ISO).
KPI	Key Performance Indicator
NGO	Non-governmental Organization
NO <sub>x</sub>	Nitrogen oxides These gases contribute to the greenhouse effect and possibly to the deterioration of the stratospheric ozone layer. At local level, they can lead to the creation of smog.
PJ	Petajoule The Joule (J) is the basic energy unit of the International System of Units (SI). It is ultimately defined in terms of the meter, kilogram and second. Peta is the metric prefix indicating 10 <sup>15</sup> times base unit (1 followed by 15 zeroes).
SO <sub>x</sub>	Sulphur oxide These gases contribute to the acid rain effect. At local level, they can lead to the creation of smog.
Sustainable Development	The concept of Sustainable Development was first conceived in 1987 by Gro Harlem Brundtland, the premier of Norway. She led the World Commission on Environment and Development and its report 'Our Common Future' defined Sustainable Development as 'meeting the needs of the present generation without compromising the ability of future generations to meet their own needs.'
WBCSD	World Business Council for Sustainable Development

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- X-ray
- Computed Tomography
- Magnetic Resonance
- Ultrasound
- Nuclear Medicine
- Medical IT
- Cardiac & Monitoring Systems
- Dictation & Speech Recognition Systems
- Remote Patient Care
- Customer Financing
- Document Management Systems
- Asset Management Services



## Domestic Appliances and Personal Care

- Shaving & Beauty
- Oral Healthcare
- Food & Beverage
- Home Environment Care
- Consumer Health & Wellness



## Consumer Electronics

- Home Entertainment Networks
- Connected Displays
- Mobile Infotainment
- Licenses

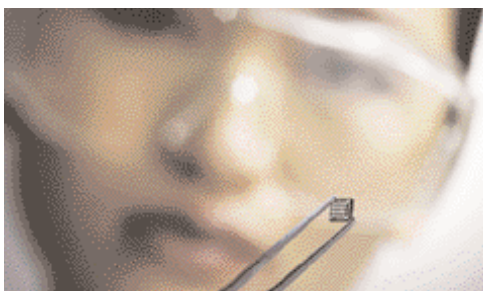


## Lighting

- Lamps
- Luminaires
- Lighting Electronics
- Automotive, Special Lighting & UHP
- Solid-State Lighting

## Semiconductors

- Consumer
- Communications
- Computing
- Automotive
- MultiMarket Semiconductors
- Foundries
- Assembly & Test
- Mobile Display Systems
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## Other Activities

- Research
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