Creating value

Sustainability Report 2005

PHILIPS

Sustainability offers a world of opportunities to improve quality of life and create value for individuals, communities and the company. We firmly believe that socially and environmentally sound behavior contributes to sustained profitable growth and value creation. That's why we are embedding sustainability throughout the organization.

Social performance
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. Our sustainable businesses improve quality of life in advanced, emerging and developing markets with solutions that deliver on our brand promise, "sense and simplicity."

New ideas,

Environmental performance
We regard environmental improvement as an opportunity for innovation. 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.

Economic performance
We are making progress on our journey to transform Philips into a truly market-driven healthcare, lifestyle and technology company. One that is capable of delivering sustained profitable growth.
We are refining our approach to sustainable business and building new markets, in keeping with our commitment to improving the quality of people's lives and creating value.

new opportunities

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.

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 2005 fiscal year, running from January 1, 2005 to December 31, 2005.

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 2005, 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.

Our *Sustainability Report 2004* covered the process of embedding sustainability in our organization. The focus of our 2005 report is on how we continue to create value in our company with sustainability as a business driver. The progress we made on our Sustainability Management Agenda over the past year is provided in this report, which features extended reporting on key issues including meeting customer needs, health and safety, environmental performance in manufacturing, EcoDesign of our products, supplier management, social investments in the communities we operate in, and the General Business Principles.

This *Sustainability Report 2005* 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 73. We will continue to improve the quality of our sustainability reporting. We are in the process of reassessing the scope of the assurance assignment for coming year(s) in order to further optimize the added value of the assurance process for our stakeholders and its contribution to internal improvements.

Readers are invited to support this improvement process with their feedback. Please contact the Corporate Sustainability Office via our website www.philips.com/sustainability or by e-mail at philips.cso@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 134 of the *Philips Annual Report 2005*. Mobile Display Systems' (MDS) activities were reclassified from Semiconductors to Other Activities effective January 1, 2005. At year-end 2005, MDS was reported as a discontinued operation in the *Philips Annual Report 2005*, in anticipation of regulatory approval of its merger with Toppoly Optoelectronics Corporation of Taiwan. Previous years have been restated accordingly. However, data on environmental and health and safety, are still covering the MDS activity for the full year 2005.

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 2005:

- 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. The consolidated financial statements in the *Philips Annual Report 2005* and the information derived for this report are prepared in accordance with generally accepted accounting principles in the United States (US GAAP). For full understanding of the financial performance, please refer to the *Philips Annual Report 2005*.

Contents

Additional information is available on our website as indicated throughout this report. Downloads of the full report are also online.
www.philips.com/sustainability/report

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 articles in this report.

Message from the President

"Our innovative products enhance people's lives, giving them easy access to quality of life benefits."

Dear Stakeholder,

On the back of a strong product line-up, we accelerated growth and increased profitability. We also executed our management agenda for the year, making Philips a more focused group, able to deliver consistent performance while continuing its transformation into a market-driven healthcare, lifestyle and technology company.

With a clear view to creating shareholder value during 2005 we took measured steps, balancing investment in growth with returning capital to shareholders. We initiated two share repurchase programs alongside two acquisitions aimed at giving us a solid footing in the key emerging growth markets of healthcare IT and solid-state lighting. We also put in place the right fundamentals to create a more competitive semiconductors business with our decision to create a separate legal structure.

We launched the second wave of our brand positioning campaign, giving our stakeholders a vision of how "sense and simplicity" is shaping our company as well as our future growth and success.

We have gained some good momentum and are confident of meeting our targets, which include embedding sustainability throughout the organization. At the same time we have been refining our approach to sustainable business and building new markets. This is in keeping with our commitment to improving the quality of people's lives with sustainability as a cornerstone of our strategy. It's about creating value.

Delivering on our commitments

We committed to a solid Sustainability Management Agenda for 2005 with a sharp focus on: measuring our Key Performance Indicators (KPIs), tracking labor indicators, risk and compliance management reporting, and developing our next four-year environmental action program. Here is what we accomplished:

Key Performance Indicators

For the first time, we identified KPIs at company level and used them to measure our performance. I am pleased to give you highlights of our achievements in several key areas:

- We more than doubled the number of Green Flagship products launched on the market compared to 2004, as well as the number of those that use less energy than their predecessors or competitors.
- We started five New Sustainable Business Initiative projects that can benefit people and contribute to our growth.
- We received a 100% return on our supplier sustainability self-assessment tool, which we use to support our supplier audit activities.

Labor indicators

Labor issues (including working hours, HIV/AIDS, remuneration, collective bargaining, non-discrimination, child and forced labor, training and education, attraction and retention) are covered in the Philips General Business Principles (GBP) and our revised GBP Directives. Further, we track our social policies by measuring employee perception related to the following key areas: inclusion, human capital development and employee engagement.

Risk and compliance management reporting

We published reported violations of the GBP on an aggregated level for the first time in our Sustainability Annual Report 2004, released in February 2005.

EcoVision III (2006-2009)

After having successfully completed our EcoVision II environmental action program, we are now beginning a new four-year program to improve our overall environmental performance. Our EcoVision III targets have been developed with an eye toward enhancing our position in environmental performance.

You will find detailed information on our performance throughout this report.

The next steps toward value creation

We have identified three important themes that we need to work on together to achieve our ambitions: Growth, Talent and Simplicity. Our commitment to sustainability supports this with a strong focus on each area.

Growing by serving the world's markets

We believe growth lies in all three parts of the global economic pyramid – the top where we have the advanced markets; the emerging markets in the middle; and the developing markets at the base of the pyramid, representing the world's 4 billion people who live on less than USD 1,500 a year. We see great potential in these markets, and we believe continuous innovation is the key to unlocking this potential and creating value, for individuals, communities and the company.

Advanced markets

Key focus areas at the top of the pyramid include healthcare, with its social benefits, and energy and material savings to help sustain the world's eco-system. In our new Center for Molecular Medicine, for example, we will detect and attack diseases at an earlier stage to enable more effective and less invasive treatment. Materials research continuously leads to better options for lighting and energy savings.

Emerging markets

In the middle of the economic pyramid, we are concentrating on new distribution channels and different business models. The latest technologies can spread fastest here. For example, these markets may become wireless societies.

Base of the pyramid

We are determining how best to develop business in these markets – how to get people the products or services they need in a viable business model that also contributes to their economic growth. That's what our New Sustainable Business Initiative is all about.

Focusing on talent

We know that we must create conditions where entrepreneurship, measured risk-taking and creativity all come together in a climate where everyone gives of their best and each person's gifts are valued. Nurturing and boosting peoples' engagement is the most important attribute of inspirational leadership. Talent means our people have an urge to belong, and the need to make a difference. That is clearly evident in our people's excitement about getting involved in our New Sustainable Business Initiative.

Experiencing simplicity

Our innovative products enhance people's lives, giving them easy access to quality of life benefits. Doing this in a simple and straightforward way illustrates what we mean by "sense and simplicity".

Sustainability Management Agenda 2006

Our 2006 Sustainability Management Agenda supports our goals, with a strong focus on:

- Achieving our KPIs, which include several new items as well as the KPIs from 2005. The additional KPIs include perception measures on employee engagement and inclusion, based on responses to our Employee Engagement Survey.
- Recognizing, measuring and leveraging the contributions of our sustainable business portfolio to our revenue stream.
- Sustaining our leading position in the environmental area with the launch of the Philips EcoVision III program.
- Furthering the roll-out of our Supplier Sustainability Involvement Program to our supply base.

"We see great potential in advanced, emerging and developing markets. Continuous innovation is the key to unlocking this potential and creating value."

Remembering a sustainable entrepreneur

Dr. Ir. Frederik Jacques (Frits) Philips passed away on December 5, 2005 at the age of one hundred. Frits Philips spent more than 40 years at the company founded by his uncle, Gerard, and father, Anton. He served as president until his retirement in 1971 and then stayed on as a member of the supervisory board until 1977.

His was a remarkable story, not only because of the things he saw and did, but also because his principles live on.

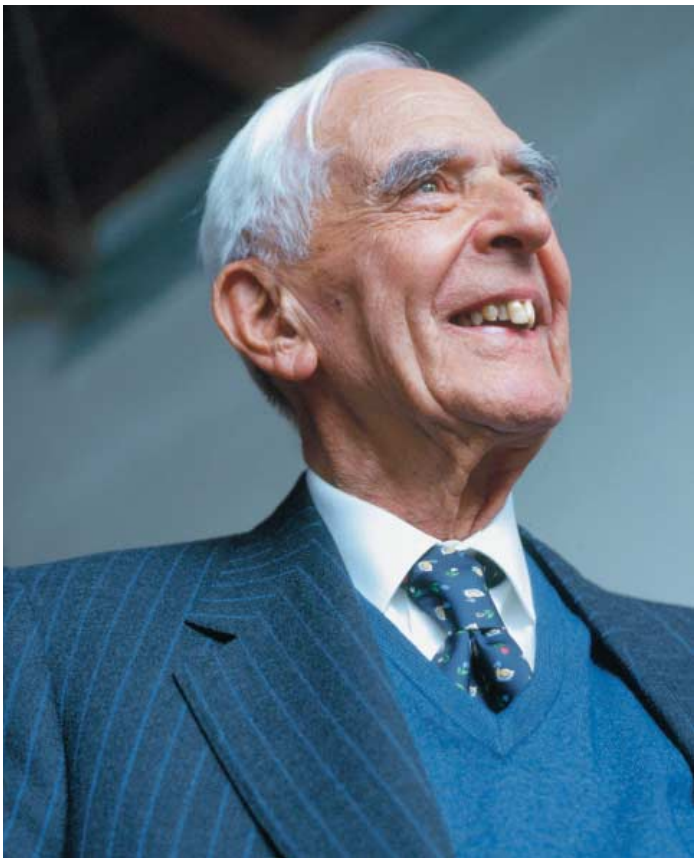
The beliefs he held – such as the importance of protecting the environment, the importance of our employees' welfare, the role of business in society – are reflected in the programs we are developing and deploying today.

In Frits Philips we lost a warm-hearted, caring man and spirited entrepreneur, whose long life was marked by a strong commitment to Philips and close involvement with the world around him. We shall always remember him with gratitude for all that he did for our company.

Gerard Kleisterlee,
President

About Philips

We remain true to the beliefs held by the entrepreneurial brothers who founded our company. Anton and Gerard Philips never lost sight of their employees or the community they came from. Sustainability is built into our heritage, our values and our commitment to improve the quality of people's lives.



A lasting legacy

Frits Philips' long life was almost entirely devoted to the company founded by his uncle and his father. He joined the family firm as an industrial engineer in 1930, shortly after completing a degree in mechanical engineering at Delft Technical University.

He made decisions not only because he saw them as good business sense, but also because he had a vision about the role of business in society that was years ahead of its time.

The 1930s influenced Frits Philips deeply. The Great Depression left him "determined that in the rest of my industrial life I would do everything within my power to avoid a recurrence of that kind of misery".

After Nazi Germany invaded the Netherlands in May 1940, Frits Philips felt that he had a duty to stay behind to try to protect the company's 19,000 Dutch workers and prevent the company from inadvertently contributing to the German war effort.

For the next four years, until the Allies liberated the Netherlands, he waged a personal war of bluff, deception, sabotage and clandestine activities, including, at the insistence of the German occupiers, opening a workshop at a new concentration camp near Vught, the Netherlands. He reasoned that by doing so he could try to protect the

Frits Philips had a vision about the role of business in society that was years ahead of its time.

Frits Philips' passion for the company was immense. And his lasting legacy is evident in this report.

Jewish prisoners' lives. To a large extent, he succeeded: of the 469 Jewish prisoners who worked there, 382 survived the war. In 1996, Frits Philips received the Yad Vashem medal from Israel in recognition of his help.

In 1961, he was made head of the company. His presidency was noted for its commitment to further expanding our presence in Asia and South America – Philips was the first European company to develop manufacturing operations in Taiwan, for example – and for the importance he attached to scientific research and development.

Frits Philips explained to an audience in 1970: "The enterprise … contributes to the prosperity and general well-being of society not only through new technological developments, but also as a source of employment and a catalyst for the development of human talents and capacities."

To do this, he believed large companies must replace "the short-term goal of maximum profit by the long-term goal of continuity so as to give increased security to employees, the providers of capital and suppliers".

It was also under Frits Philips that the company's plants and related companies were ordered to introduce an active and effective environmental policy.

His passion for the company was immense. And his lasting legacy is evident in this report.

Key figures 2005

Sales[1]	EUR 30,395 million
Market capitalization[2]	EUR 31.5 billion
Net income[1]	EUR 2,868 million
Net income per common share[1]	EUR 2.29
Earnings before interest and tax[1]	EUR 1,779
EBIT as % of sales[1]	5.9%
Net operating capital[2]	EUR 8,043 million
Stockholders' equity[2]	EUR 16,666 million
Net debt: Group equity ratio[2]	(5) : 105
Research & development expenditures[1]	EUR 2,559 million
R&D expenditures as % of sales[1]	8.4%
New patents filed in 2005[1]	2,854
Patent portfolio (families)[2]	23,062
Multinational workforce[2]	159,226 FTEs
% Male-female workers[2]	62.3% : 37.7%
% Female executives[2]	5%
Lost Work Time rate[1]	2%
Lost Workday Injuries[1]	7/1,000 FTEs
Global Warming Potential[1]	929 kilotons CO_2 equivalents
Direct CO_2 emissions[1]	343 kilotons
Energy consumption[1]	28.4 PJ
Water intake[1]	16 10^6 m^3
Total waste[1]	151 kilotons
Packaging[1]	246 kilotons
Number of Green Flagship products[2]	50
ISO 14001 certification[2]	93%
Number of countries with sales and service outlets[2]	150
Number of manufacturing sites[2]	135
Number of suppliers[2]	25,500

[1] Full-year 2005 [2] Year-end 2005

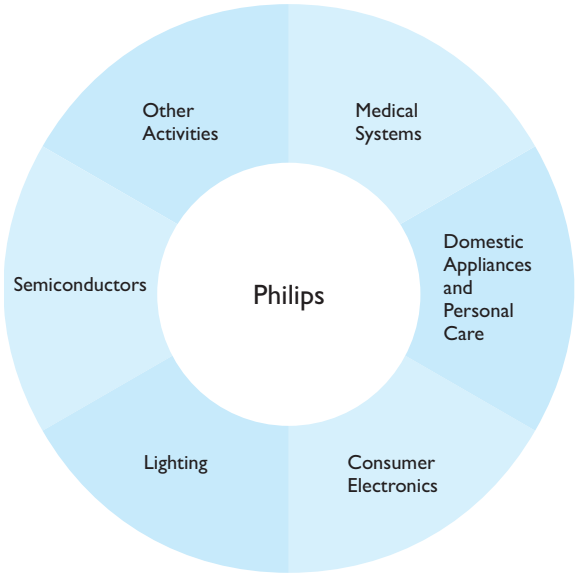
Our organization

'Royal Philips Electronics' is the parent company of the Philips Group. Its shares are listed on the stock markets of Euronext Amsterdam and the New York Stock Exchange. The management of the Philips Group is entrusted to the Board of Management under the supervision of the Supervisory Board. The Group Management Committee, consisting of the members of the Board of Management, chairmen of the operating divisions and certain key officers, is the highest consultative body within Philips, and its tasks are to ensure that business issues and practices are shared across Philips, to implement common policies and to foster the spirit of collaboration required to unlock Philips' full potential.

The Supervisory Board has decided to propose to the 2006 General Meeting of Shareholders to appoint the current CEOs of the operating divisions as members of the Board of Management, effective April 1, 2006.

Business overview

Philips' activities – focusing on the interlocking domains of healthcare, lifestyle and technology – are organized in five product divisions (see diagram below), each of which is responsible for the management of its businesses worldwide.



Furthermore, Philips engages from time to time in cooperative activities with other companies. These are included in the section 'Our cooperations' in the Annual Report on page 50-51. Strategic alliances are also important to Philips. One example is its partnership with InBev, one of the global leaders in the beer market, for a home draft beer system, PerfectDraft.

Participations

Philips is involved in the following joint ventures and participations:

LG.Philips.LCD	32.9%
LG.Philips.Displays	50.0%
TSMC (Taiwan Semiconductor Manufacturing Co. Ltd.)	16.4%
FEI Company	25.0%
InterTrust Technologies Corporation	49.5%
Philips Medical Capital (USA, Europe)	40.0%
TPV Technology Limited	15.0%

At year-end 2005, the Corporate Venturing portfolio comprised some 10 companies in which we have a minority stake and, in some case, an active business relationship.

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. Our market positions are (value based, 2005):

- Global leader in Lighting
- Global leader in Medical Imaging Equipment
- Global leader in Male Shavers
- Market leader in Oral Health Care in the USA
- Market leader in coffee makers in Europe

Brand equity

The BusinessWeek/Interbrand 2005 ranking of the Top 100 Most Valuable Global Brands placed Philips at number 53, a 12-place jump from the previous year.

Risk management

You will find an overview of our approach towards risk management and business control, followed by a description of the nature and the extent of its exposure to risks, in the *Philips Annual Report 2005*. The risk overview is not exhaustive. Some risks not yet known to Philips or currently believed not to be material could later turn out to have a major impact on our businesses, revenues, income, assets, liquidity or capital resources.

The risk factors should be considered in connection with any forward-looking statements.

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Philips Business Control Framework

Risk management forms an integral part of business management. The company's risk and control policy is designed to provide reasonable assurance that strategic objectives are met by integrating management control over the company's operations, by ensuring compliance with legal requirements and by safeguarding the integrity of the company's financial reporting and its related disclosures. It makes management responsible for identifying the critical business risks and for the implementation of fit-for-purpose risk responses. Philips' risk management approach is embedded in the areas of corporate governance, Philips General Business Principles and Philips Business Control Framework and in the actual periodic business planning and review cycles.

Corporate governance

Corporate governance is the system by which the company is directed and controlled and Philips believes that good corporate governance derives from, amongst other things, careful internal controls and high ethical standards. Risk management is a well-established part of our corporate governance model.

The quality of the company's systems of business controls and the findings of internal and external audits are reported to and discussed in the Audit Committee of the Supervisory Board. Internal auditors monitor the quality of the business controls through risk-based operational audits, inspections of financial reporting controls and compliance audit. Audit committees at division, business and regional levels meet on a regular basis to address weaknesses in the business control infrastructure as reported by the auditors, and to take corrective action where necessary. These audit committees are also involved in determining the desired internal audit coverage. An in-depth description of the Philips corporate governance model can be found on page 218 of the Annual Report 2005.

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Meeting of Shareholders

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 or shareholders in accordance with the provisions of the company's articles of association. The General Meeting of Shareholders is held no later than six months after the end of the financial year. More details are discussed in the Annual Report.

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Philips General Business Principles

The Philips General Business Principles (GBP) set out guiding principles on integrity and ethics in business conduct. They govern the company's business decisions and actions throughout the world and apply equally to corporate actions and to the behavior of individual employees in conducting company business. The intention of the GBP is to ensure compliance with laws and regulations, as well as with the company's norms and values for 'doing business'.

GBP governance

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.

Responsibility for compliance with the GBP rests first and foremost with the management of each business. Confirmation of compliance with the Principles is an integral part of the annual Statement on Business Controls that has to be issued by the management of each organizational unit.

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Country Compliance Officers have been appointed in 73 countries where Philips has a presence. Additionally local Product Division Compliance Officers have been appointed at major sites.

Revised GBP Directives

Based on our continuous tracking of societal trends and developments, in October 2005 the Board of Management adopted a revision of our GBP Directives, which provide detailed guidelines to drive the practical deployment of the General Business Principles. The revised Directives include topics such as employee relations, remuneration, working hours, employee development and harassment. Further, a new Directive was added concerning Internet, intranet and e-mail use. In December 2005, following approval by the Supervisory Board, these revised Directives were implemented in supporting processes and procedures, such as websites, self-assessment tools, internal reporting mechanisms as well as complaint handling procedures.

Web-based GBP training

Following a successful pilot for our Medical Systems employees in the United States, the Board of Management decided to roll-out new web-based GBP training company-wide. Based on our employee population, the International-English version was translated into the following nine languages: Chinese, Dutch, French, German, Hindi, Polish, Latin American Spanish and Portuguese. Other major languages will follow in 2006.

Additionally, the GBP will continue to be communicated by various means, including our dilemma-training casebook, the incorporation of the GBP into the employment contract and our introduction programs for new employees.

Plans for 2006 and 2007 include refresher courses and global awareness training for the new GBP Directives.

One Philips Ethics Line introduced

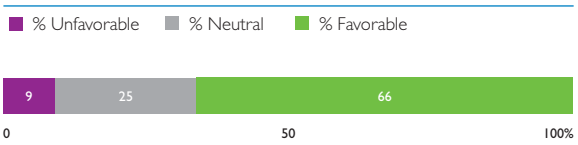
The new One Philips Ethics Line is designed to make it easier for employees to report violations of the GBP and related policies. We began rolling out the Ethics Line in October 2005 with Philips-wide implementation planned for mid-2006.

Once this One Philips approach is fully operational, we will have a single global reporting process and toll-free country-specific numbers that anyone who suspects a violation can call. Employees can speak anonymously and in complete confidence with trained communications specialists in a call center managed by a specialized third-party company.

In those European countries where required by local legislation on employee privacy, we are working with employee representation bodies and governmental agencies.

Philips strives to create an environment in which employees feel comfortable to report GBP non-compliances and are confident that reported allegations are taken seriously. Therefore, we have a Whistleblower policy in place, describing the investigation procedure for suspected violations and ensuring the complainant's confidentiality to the extent possible. Employees are entitled to protection from retaliation for making a complaint in good faith.

Employees' response to:
'Philips shows a commitment to ethical business decisions and conduct'



Source: Philips Employee Engagement Survey 2005
Number of responses: 93,947

Reported complaints

In 2005 a total of 318 concerns were raised, including those arising from our supplier sustainability audits, compared with 232 in 2004. Further, this year shows a nearly 20% increase in concerns that relate to employees' work environment. While there are multiple factors that may have been of influence, we believe that the extended scope of the GBP, especially in the employee domain, and the introduction of the Ethics Line may have contributed to both increases.

To further improve on the uniform and correct handling of complaints related to working conditions, detailed guidelines for Philips Compliance Officers and HR managers have been made available on our intranet. Corrective actions taken in 2005 include dismissal, warnings, job changes, and individual as well as departmental training and education.

Improved monitoring

Working in close cooperation with Internal Audit, the GBP Review Committee has reworked its risk profiling and analysis tool to strengthen monitoring of GBP compliance at our organizations around the world. This updated Risk Index will be used as a tool to identify audits, based on internal and external indicators.

Breakdown of alleged violations of the General Business Principles
% of total

Chapters		2004	2005
1	General commitment		
1	General commitment	6.3	2.2
1.1	Human rights	0.0	0.0
1.2	Child, bonded and forced labor	0.0	0.0
1.3	Free market competition	3.0	0.0
1.4	Product safety	0.4	1.1
1.5	Privacy	0.4	0.5
1.6	Environmental protection	0.0	0.5
	Total	10.1	4.3
2	Commitment towards customers		
	Total	1.9	0.0
3	Commitment towards shareholders		
	Total	0.4	0.0
4	Commitment towards employees		
4	Commitment towards employees	2.6	6.7
4.1	Right to organize	0.0	1.1
4.2	Health and safety	0.7	0.8
4.3	Equal and fair treatment	26.1	34.1
4.4	Wages and payment	0.0	5.4
	Total	29.4	48.1
5	Commitment towards suppliers and business partners		
	Total	0.0	8.9
6	Assets and information		
6.1	Use and protection of assets	23.9	19.6
6.2	Improper disclosure	3.0	4.6
6.3	Insider trading	0.0	0.0
	Total	26.9	24.2
7	Business integrity		
7.1	Bribery; records of transactions	20.1	11.0
7.2	Third-party interests	11.2	2.2
7.3	Political payments	0.0	0.5
	Total	31.3	13.7
8	Observance of the General Business Principles		
8.1	Sanctions	0.0	0.0
8.2	Whistleblower policy	0.0	0.8
8.3	Compliance	0.0	0.0
	Total	0.0	0.8
	Overall total	100.0	100.0

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Privacy

We believe it is important to inform our consumers and employees about how their personal data are used, and to gain their trust by keeping their personal data confidential and secure. As one of the first companies in the world, Philips has drafted a Code of Conduct, which creates a Safe Haven for personal data within the Philips Group of Companies worldwide. The Philips Privacy Code will be fully integrated with the Philips General Business Principles. The final draft has been submitted for approval to the various Data Protection Authorities in Europe and we expect it will be rolled out in 2006.

We paid special attention to the protection of employees suspected of fraud or misconduct. Rules of conduct for internal investigations, as well as the procedures for anonymous reporting via the One Philips Ethics Line, were scrutinized and adapted to ensure the processing of data in such procedures fairly protects the interests of all parties concerned.

As a leading technology provider, we are working to find technical solutions to privacy issues. Philips Research has developed a solution for privacy protection in the Connected Home. Secure home servers allow private users to control the sharing of protected personal content with other people over open networks like the Internet. This way they are able to securely share photos with family members or friends, or share sensitive medical information with their family doctor or teachers. Philips Research will continue to develop privacy solutions for various technologies, such as Radio Frequency Identification (RFID) – which continues to be a dominant topic in the global privacy discussion – medical information systems and ambient home applications.

Acting on our commitment to help legislators understand the promising RFID-technology, Philips led the industry response to the public consultation paper on RFID and privacy of the joint European Data Protection Authorities ('the Article 29 Working Party'); testified before the OECD Committee on Information, Communications and Computers Policy at its RFID Foresight Forum; and joined several public discussions on national level in the United States, Germany and the Netherlands. Further, we participate in various initiatives to promote responsible use of RFID technology, including those of the International Chamber of Commerce, EPCGlobal and the Smart Card Alliance.

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Sustainability at Philips

Sustainability offers a world of opportunities to improve quality of life and create value. At Philips we believe the way to explore these opportunities is by embedding sustainability throughout the company, ensuring that it is woven into our strategy and culture.

Embedding sustainability at Philips

To drive sustainability throughout the organization, Philips uses an embedded model approach for all parts of the business system. You will find examples of how we are doing just that in this report and on our web pages.
www.philips.com/sustainability/report

Sustainability governance

Sustainability is governed within our company by:

- The Philips Sustainability Board at Group level.
- Sustainability Councils in our product divisions, regions, India and China, and in Philips Research.

The sustainability network includes employees in nearly all functional areas, including Communications, Global Marketing Management, Finance, Investor Relations, Supply Management, Human Resource Management, Legal, Mergers and Acquisitions, Design, Strategy, Quality and Research.
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Key Performance Indicators

To track our progress on the major issues regarding sustainability, we are continuing to focus on the Key Performance Indicators (KPIs) we started measuring in 2005. These KPIs have been extended to include more subjects for 2006.

Key Performance Indicators		2005 Objective	2005 Actual	2006 Objective
Social				
Health and safety	Level of absenteeism (%)	2%	2%	2.0%
	Number of lost workday injury cases/1,000 FTE	7	7	6.5
Human capital	Women at executive level (%)	6%	5%	6%
	Asians at executive level (%)	7%	8%	9%
	Inclusion Index (% favorable: 2004 = 54%)			> Level 2004
	Employee Engagement Index (% favorable: 2004 = 58%)			> Level 2004
Business				
New Sustainable Business Initiative	2005: number of new projects **2006: succesful results of running projects**	3	5	2
	Number of people that benefit from projects	15,000	20,000	50,000
Environment	2005: number of Green Flagship products with energy consumption as one of the focal areas **2006: number of new Green Flagships**	5	34	35
Sustainable business	**Sales from sustainable business**			3%
Supplier involvement	2005: returned sustainability self-assessments **2006: on-site assessments of critical suppliers (%)**	100%	100%	20%
Communication				
Stakeholder dialogue	2005: number of countries with monitoring program **2006: quarterly issue-grid reporting**	40	40	Start Q2
Internal communication	Sustainable messaging measured amongst employees as favorable (%)	53%	62%	70%
External communication	Number of favorable clippings in top level printed media	50	322	> Level 2005
Reporting				
Verification	Level of assurance	moderate	moderate	moderate
Compliance	**Comparative (2005 vs 2004) reporting of alleged violations and number of corrective actions in 2005**			In report 2005
Performance	**Quarterly results reporting on KPIs**			In 2006

Bold = New for 2006 Realized Not realized

Recognition

Our sustainability performance is externally recognized in a variety of ways, examples of which are highlighted here and on our website.

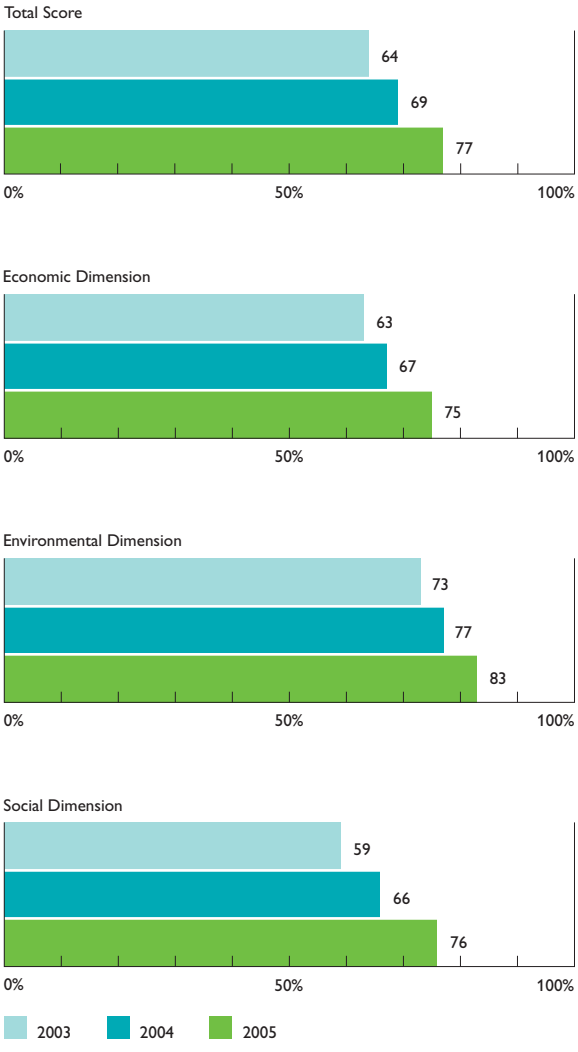
www.philips.com/sustainability/report

Dow Jones Sustainability Index

We are proud that we continue to be included in the Dow Jones Sustainability World Index for the third year running. The Dow Jones Sustainability World Index comprises more than 300 companies that represent the top 10% of the leading sustainability companies out of the biggest 2,500 companies in the Dow Jones World Index.

We are also listed in the Dow Jones STOXX Sustainability Index and the Dow Jones EURO STOXX Sustainability Index, which comprise the leading companies in terms of sustainability from Europe and the Eurozone.

Philips' Dow Jones Sustainability Index scores



Global 100

Philips was among the Global 100 Most Sustainable Corporations in the World, a global business ranking unveiled at the World Economic Forum in Davos, Switzerland, in January 2005. From a pool of over 2,000 firms representing such global indices as the S&P 500, FTSE 350 and EURO STOXX, the top 100 were selected on their ability to manage strategic opportunities in new environmental and social markets.

Amsterdam Stock Exchange (AEX)

Philips once again ranked top in sustainability among companies on the Amsterdam Stock Exchange (AEX). The Dutch Sustainability Research report uses seven criteria in its assessment, including company ethics, environment, corporate governance, employee engagement and societal engagement.

FTSE4Good

The FTSE4Good Index Series has been designed to measure the performance of companies that meet globally recognized corporate responsibility standards, and to facilitate investments in those companies. We are proud to continue to be included in this index.

Memberships

Philips has been a member of the World Business Council for Sustainable Development (WBCSD) since 1993. The WBCSD is a coalition of 180 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. The organization and its members also benefit from a global network of 50 national and regional business councils and partner organizations involving some 1,000 business leaders globally.

World Business Council for Sustainable Development

GRI

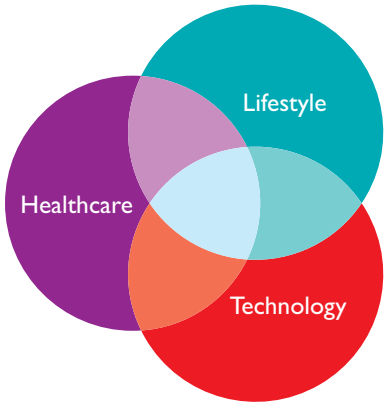
Philips is an organizational stakeholder for the Global Reporting Initiative (GRI). According to GRI, organizational stakeholders "are a critical element in GRI's governance structure and the foundation for sustaining the GRI as an open, democratic and global institution".

Sustainability... Creating value

For over 110 years, since our founding as a manufacturer of light bulbs in 1891, we have understood that the simultaneous pursuit of business interest and socially and environmentally sound behavior is critical to success. Putting people at the center has led to meaningful innovations that enhance quality of life with breakthroughs in, for example, medical imaging, television, lighting, optical technology and integrated circuits. Improving people's quality of life creates value for individuals, communities and the company.

Our scope: healthcare, lifestyle and technology

In a world where technology increasingly touches every aspect of our daily lives, we are focusing our activities on the overlapping domains of healthcare, lifestyle and enabling technology.



Thanks to our combination of consumer insights and technology know-how, we are well positioned to deliver the kinds of solutions that will delight consumers and customers and secure leadership positions in these markets. We also see tremendous potential for new product/service categories in the areas where the domains converge.

Our mindset and way of working: One Philips

Inspired by our mission to improve the quality of people's lives through the timely introduction of meaningful technological innovations, and resolved to exploit the potential outlined above, we have embarked upon a journey of transformation as fundamental as anything the company has experienced in its history.

The objective? To create One Philips – a focused, market driven company geared to delivering sustained profitable growth.

One Philips is all about unlocking synergies. The belief that by working together we can create more value than the sum of the parts, … that by working together we can achieve further growth at the interfaces between the three domains. In essence, One Philips is a mindset and a way of working focused on maximizing value creation for the company and our customers by leveraging our competencies and resources across the areas of healthcare, lifestyle and technology.

The One Philips culture is the sum of how we conduct ourselves, what we believe in and how we work within the company and interact with our customers. Delight Customers, Deliver on Commitments, Develop People and Depend on Each Other are the values that guide us in our everyday working lives.

One Philips is a mindset and a way of working focused on maximizing value creation for Philips and its customers by leveraging our competencies and resources across the areas of healthcare, lifestyle and technology.

"Sense and simplicity" is our brand promise. We are committed to designing our products, systems and services around the people who will be using them. So, no matter how advanced they are, they make sense and are simple to use.

Our brand promise: "sense and simplicity"

In 2004 and 2005 we entered a key phase in our transformation towards One Philips with the launch and roll-out of our new brand positioning and our brand promise of "sense and simplicity". We firmly believe that simplicity is the key to successful technology. We want to offer our customers straightforward solutions that meet their needs and wishes. Accordingly, we are committed to designing our products, systems and services around the people who will be using them. So, no matter how advanced they are, they make sense and are simple to use. But "sense and simplicity" is much more than simply an advertising campaign – it defines the criteria against which we gauge everything we do and make. It also expresses how we want to be perceived by all our stakeholders: open and transparent, approachable, easy to do business with.

Our strategy

We see tremendous potential in both developed and emerging markets and we believe continuous innovation is the key to realizing this potential, helping us to transcend the innovation-to-commoditization cycle and helping us to achieve sustained profitability.

True innovation will, we expect, move us beyond incremental improvement to create new product/service categories that redefine the borders of our industry and generate new growth and profitability.

We have defined a six-point strategy for attaining our goal:

- 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 intellectual property position;
- Strengthen our leadership competencies;
- Drive productivity through business transformation and operational excellence.

Our philosophy

Understanding our markets and the needs of our customers is our starting point for innovation and entrepreneurship. Reflecting our commitment to "sense and simplicity", we are continuing to enrich our design process by integrating established design skills with input from other disciplines such as the human sciences, technology and business, while at the same time maintaining our investment in technology leadership. And we are continuing to engage in partnerships – in new fields and in new ways, for example by partnering with non-governmental organizations in our New Sustainable Business Initiative projects.

It is our belief that socially and environmentally sound behavior contributes to sustained profitable growth and value creation. 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.

Only our people can realize our strategy, sustain and develop our capabilities and ultimately deliver on our promises to our external stakeholders. Accordingly, we are further developing and leveraging our people competencies, e.g. embedding diversity and inclusion in career development programs. This is essential in order to secure the quality of leadership required to take our company forward – leaders who pursue market insight, establish innovative strategies, inspire commitment, leverage capabilities, champion people's growth and drive relentlessly for results.

Sustainable business

Sustainability is built into our heritage, our values and our commitment to improve the quality of people's lives. Today we see sustainable business as an opportunity to contribute to sustained profitable growth and value creation.

Defining sustainable business

We define 'sustainable business' as a Philips product or service that takes credible and sustainable benefits into account. These benefits create both financial and non-financial value, contributing to financial return on investment (ROI) for our company, as well as financial and non-financial returns on investment for our customers. Non-financial ROI include social and environmental benefits that can improve quality of life in many different ways. Our sustainable business definition can be applied to products and services in all market segments of the economic pyramid – advanced, emerging and developing.

Using a sustainable product can have one or more environmental benefits and/or one or more social benefits. Trends and market insights are used to identify the consumer needs and emotional appeal connected to those benefits, and how they can be communicated to consumers and customers, and the public at large. Providing access to those benefits in a simple and straightforward way with Philips technology gives our customers many opportunities to experience what we mean by "sense and simplicity".

We are refining our approach to sustainable business and building new markets, in keeping with our commitment to improving the quality of people's lives and creating value.

At Philips, sustainable business addresses three areas: new sustainable business, green products and existing products.

New sustainable business

A new sustainable business is a product or service utilizing new technology or existing technology applied in a new way. At the outset, we use market insight to identify quality of life benefits and how our technology can provide simple access to them. Improving healthcare or bringing rechargeable lighting to areas with no electricity, are just a couple of examples. Our New Sustainable Business Initiative is discussed later in this chapter.

Green products

Green products or product groups are considered sustainable businesses when we know that the environmental improvement is a quality of life benefit, based on market research. Products that reduce global warming, for example, resonate with consumers. Within the green product category, Green Flagships are our top tier products. (See pages 54-57.)

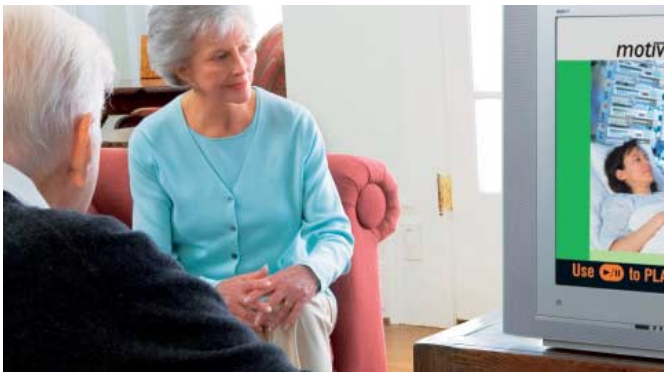
Existing products

This is a product or service already on the market that implicitly improves quality of life and market insight shows this improvement is of interest to the end-user. An example would be superior ergonomics that benefit technicians using our ultrasound equipment. Other examples are included in the following pages.

Put simply, sustainable business is a One Philips approach to contribute to our growth strategy, support our brand positioning and live up to our mission to improve quality of life with our technology. To do this, we monitor and analyze societal trends, focusing on those issues that mirror our core competencies.

www.philips.com/sustainability/report

We are extending our knowledge of consumer electronics technologies for the digital home into the realm of healthcare. Motiva enables patients and their doctors to transmit medical data via the patient's TV.



Benefiting patients and healthcare professionals

Our objective is to be the patient-focused medical solutions provider, helping the customer perform better in the healthcare sector by offering solutions that are more patient-friendly. Drawing upon expertise from across the company and beyond, we are working together to create innovative solutions that are designed around the needs of both patients and healthcare professionals.

Healthcare in the digital home

We are creating partnerships to serve both medical professionals and patients. Working with a cable company in the United States, Philips allows patients suffering from heart disease to be monitored from home. The system, called Philips Motiva, uses secure broadband technology to connect patients in the comfort of their own homes to the care providers monitoring their condition. In June 2005 we started the first 12-month pilot study in Europe with Philips Motiva, working with one of the largest healthcare insurance companies in the Netherlands.

Motiva bridges our presence in the home and in healthcare. In effect, we have created a new category driven by the Connected Planet vision, with a different revenue model based on long-term partnerships and a different role for Philips – as a service platform provider.

Motiva aims to improve the quality of life for the chronically ill while helping drive down the costs of managing chronic disease. Clinical evidence shows that if you can bring people from the hospital back to their homes quicker, not only do you save costs, but also people recover better. Motiva empowers patients to take a more active role in their own healthcare.

Patient-friendly diagnostics

Our alliance with Schering AG builds on our patient focus of coming out with advanced, patient-friendly approaches to preventing and treating serious diseases like breast cancer. With a focus on the prevention and treatment of breast cancer to begin with, we will work together to develop more patient-friendly ways of screening and significantly reducing the need for expensive and uncomfortable invasive investigations such as biopsies.

The alliance's first development project will combine an optical dye called omocianine (SF-64) from Schering for the diagnosis of breast cancer, currently in Phase I trials, with an enhanced mammography device developed by Philips. We will also explore the emerging field of molecular imaging, looking at how to develop dyes that can potentially target breast tumors at the molecular level.

According to health services company Imaginis Corporation, breast cancer is the second leading cause of cancer deaths in women today (after lung cancer). The World Health Organization estimates that more than 1.2 million people around the world will be diagnosed with breast cancer this year, with the number of deaths among women expected to exceed 40,000 in the United States alone. Death rates from breast cancer did decline significantly between 1992 and 1996, according to the American Cancer Society, and medical experts attribute the decline to earlier detection and more effective treatments.

Quality living – by design

We apply our shared understanding of how people interact with technology to design advanced yet user-friendly products and solutions that meet their everyday needs and enhance their quality of life.

Relaxed TV viewing

Our Cineos FlatTV with Ambilight is the next step in the evolution of television. Combining expertise from Consumer Electronics, Lighting and Research, Ambilight technology analyzes – in real time – the incoming television signals and projects lighting onto the wall behind the set, enveloping the viewing environment in color that matches the content on the TV. The Ambilight effect is projected from the back of the flat TV monitor and automatically changes colors and intensities to match the picture on the screen.

Ambilight also offers stress-relief for the eyes. Tests show that by providing a well-balanced amount of light behind the TV set, the range in motion of the iris muscle is reduced. This leads to more relaxed viewing. And it eliminates the need for additional lighting while watching TV.

Our Cineos FlatTV features innovations that make on-screen images even more realistic. The unique Ambilight 2 backlighting system provides well-balanced light, offering stress relief for the eyes.

Technology that makes a difference

We see technology as an enabler. If it improves people's lives, a smart application of technology can be as 'advanced' as the technology itself.

Working to improve a patient's daily life

Scientists at Philips have made progress on a range of Personal Healthcare (PHC) solutions for measuring medically relevant parameters outside the hospital. These solutions rely on 'invisible' Ambient Health Sensors, which continuously monitor medical condition and fitness. PHC applications are currently limited by the lack of suitable sensors for personal use, mainly due to concerns about ease-of-use and cost. The challenge is to bring sensors into a patient's daily life, for example in clothing or furniture, under ill-defined measurement conditions.

In 2005 we demonstrated the possibilities of using these solutions in a chair with integrated intelligent electronics that automatically detects heart rate. The person needs no additional body-worn devices and only has to sit and be at rest to produce a stable reading. The electronics in the chair detect heart rate and transmit this information via a Bluetooth-link to a user interface. The measurements are unobtrusive and safe: medically relevant parameters are gathered with a minimal impact on a person's quality of life. Advanced low-power wireless technology and intelligent power management systems ensure that they can operate for months or years on tiny batteries.

New Sustainable Business Initiative

We are exploring new approaches to doing business – approaches that embrace sustainability as a framework for generating new revenue, increasing shareholder value, heightening stakeholder satisfaction and enhancing corporate brand reputation by living up to our brand promise, "sense and simplicity". At Philips, this exploration into new ways of doing business is at the heart of our New Sustainable Business Initiative (NSBI). Our focus is on improving quality of life in all markets.

Charity or New Sustainable Business?

Our various NSBI projects in developing markets differ significantly from philanthropic activities. New sustainable business initiatives are entrepreneurial activities aiming to create both social and economic returns on investment, even though there may be different pay back times for each dimension.

Open Innovation

Rick Harwig
CEO and Executive Vice President
Philips Research
Member of the Sustainability Board

We continuously think and act beyond our own boundaries. In a spirit of what is called Open Innovation, we choose best-in-class academic and industrial partners who have competencies and interests that complement our own. We join forces with industry peers on standardization and create momentum in the future directions of technology we jointly aspire to. And we are active in establishing strong local networks of leading industries and research institutes that help top technology regions and developing regions to grow.

For example, we signed a research and education agreement with the Technical University of Eindhoven and Zhejiang University, China. With this agreement, we want to foster a new culture of technical excellence through the creation of a 'brain bridge' between eastern and western universities and companies, and support China's efforts in creating the high-quality homegrown scientists and engineers the country will need to sustain its growing economy.

Like so many other business concepts, the trick with Open Innovation is knowing when and where to apply it. One way we can gain an advantage from Open Innovation is in molecular imaging and diagnostics, which is a new field of opportunity. Applying our vast knowledge in imaging and micro-systems technologies requires cooperation with bio-pharmaceutical companies. This seems to contradict standard models for takeovers and acquisitions, but the result is the ability to play with a wide variety of ideas, diseases, drugs and imaging modalities, which will lead to opportunities for the companies that are vibrant enough to turn new innovations into products.

Open Innovation is about global cooperation. As we move forward, there will be more and more interplay between countries and regions worldwide. Although in some cases this will make operational issues more complex, it will provide us with many challenging opportunities for innovations that are key to a more sustainable future. Through Open Innovation, we can all benefit and be sustainable.

Areas we explore

With our NSBI, we explore areas that are in line with our company focus on healthcare, lifestyle and technology, and our mission to improve quality of life. We also take into the account the UN Millennium Development Goals that relate to our company's know-how and capabilities.

As a result, these following themes are considered when we develop a sustainable business case:

- Health and wellbeing – Enhancing access to physical health and personal care, leveraging medical professional solutions, home applications and telemedicine services.
- Clean energy and lighting – Increasing access to clean energy and lighting, leveraging the combination of eco-efficient lighting products, solar power systems, digital applications and networking technologies.
- Fresh water and air purification – Increasing access to safe drinking water and indoor clean air, leveraging purification technologies.
- Food preservation and processing – Facilitating access to fresh food, leveraging off-grid applications for food preservation and preparation. (Off-grid applications do not use electricity from large power plants. Rather, where needed, electricity can be generated by means of renewable resources like solar, wind, water, bio-mass or human-powered solutions.)
- Knowledge distribution and sharing – Bridging the gap between digital haves and have-nots by enabling access to information and knowledge sharing, leveraging our display, connectivity and networking know-how.

Addressing the needs of the 1 billion people on the planet who have no access to safe drinking water, we are working on several technological solutions for water purification.

A world of opportunity

We're looking at interesting projects for new and emerging markets, including the base of the economic pyramid. In 2005 we started the following five New Sustainable Business Initiatives.

Sustainable lighting

Simple and cost effective lighting is a basic need in parts of the world where the power grid is unreliable. Much effort has gone into establishing people's lighting needs and finding ways to address them. Lighting beyond sunset will extend productive working hours and enable students to study in the evening. Reducing the use of conventional polluting sources of light, like kerosene, will improve health and hygiene. Challenges lie ahead in finding a business model that effectively brings quality and affordable lighting to people in the developing world.

Smokeless cooking

By using up to five times less wood than traditional stoves, our smokeless wood stove can save people the time of gathering wood and the money to buy it. Since smoke and other emissions are reduced up to a factor of 10, a very positive impact on health is expected. Some 1.6 million people die each year from smoke-related diseases caused by cooking fires. In the spirit of Open Innovation, we are sharing our ideas with non-governmental organizations and other partners.

Water purification

Providing affordable community and household water purification solutions addresses the needs of the more than 1 billion people – 20% of the planet's population – who have no access to safe drinking water. One of our enabling solutions is the Philips TUV lamp, which emits in a part of the ultraviolet (UV) spectrum that is highly effective in inactivating bacteria. Our UV light makes drinking water safer and improves its taste, odor and clarity. It can also be used to purify air and sterilize surfaces.

Improving vision

Making affordable spectacles available will improve poor vision due to uncorrected refraction. This can prevent people from developing permanent blindness, as well as enhance literacy and job opportunities.

Oral cancer diagnosis

We are working to provide early oral cancer diagnosis and care for less cost, using our know-how in consumer electronics and healthcare.

Our DISHA project brings high quality diagnostics and the resulting healthcare to underserved rural communities in India.

Digital connectivity

Our Voices in Your Hand pilot in Recife, Brazil, concluded at the end of 2005. Designed to bring digital connectivity to people at the base of the economic pyramid, Voices in Your Hand allows people to communicate with others and have access to information even though fixed-line or wireless phones are beyond their economic reach.

We are analyzing the results of the pilot. High costs are a barrier to large-scale implementation, so we are considering alternative business models to determine feasibility of scaling up.

The pilot included extensive research to determine the project's social impact. Voices in Your Hand improves quality of life, providing information and entertainment, as well as improving self-esteem and self-confidence.

Setting a new direction in India

DISHA is the acronym for Distance Healthcare Advancement and also means "direction" in Hindi – appropriate for this pioneering new direction Philips has set with our DISHA pilot and the life transforming direction for the people it promises to impact.

Using vans equipped with diagnostic suites and connectivity, DISHA brings high quality diagnostics and resulting healthcare to underserved rural communities. Targeting an emerging market, it's a cross-divisional project that also involves non-Philips partners.

Based on what we have learned since this pilot launched in July 2005, we have decided to expand in 2006. Our plans call for a second pilot to help us further develop and refine the project design, hardware configurations and service model, as well as establish sustainable revenue streams on a wider spectrum. The next phase in the pilot will include another 'hub' van and smaller vehicles that can more easily navigate in rural areas.

We will continue to strengthen our existing public-private partnerships and develop new ones in microfinance and micro health insurance.

www.philips.com/sustainability/report

Business, not charity

K. Ramachandran
CEO
Philips India

Telemedicine projects are not new in India. But DISHA breaks new ground for many reasons. It is mobile, offers multiple diagnostic modalities, includes satellite connectivity to a remote specialty hospital, has four strategic public and private partners including Philips, and aims to build a sustainable business model. To the best of our and our partners' knowledge, no other telemedicine project has all these characteristics.

For me, building a sustainable business model is most crucial. DISHA isn't only about corporate social responsibility and is not at all about corporate philanthropy. It is about creating an economically viable business model with reasonable profits for all partners in the value chain, quality of life benefits for the consumers served and the possibility of community ownership.

The biggest learning from the first six months of operation is that health-seekers' interest has been overwhelming. This has highlighted the even greater need for trouble-free operation, ruggedness and high uptime of the teleclinical van, including connectivity and the availability of the medical staff. Also, trust between partners is even more vital than contractual relationships, and this type of project requires strong project management.

Re-packaging technologies for emerging markets

I describe what we are doing as exploring ways to unleash the potential of Philips' capabilities and technologies by re-packaging them into value propositions for consumers in emerging markets. International companies develop and bring to market 90% of their products for the affluent 25% of the world's population. The benefits of technology simply aren't available to most people in the world, in countries like India, China, large parts of South Asia, South America and Africa.

We at Philips are working to make the benefits of our technology available, accessible and affordable.

Innovative value propositions

Philips has been in India for 75 years, and we're a highly trusted, reliable brand and a household name. We would like to become a center of competence in innovating value propositions and business models for emerging markets. To leverage the power of our technologies to create accessibility, availability and affordability – not just for India, but for all emerging economies.

Highlights

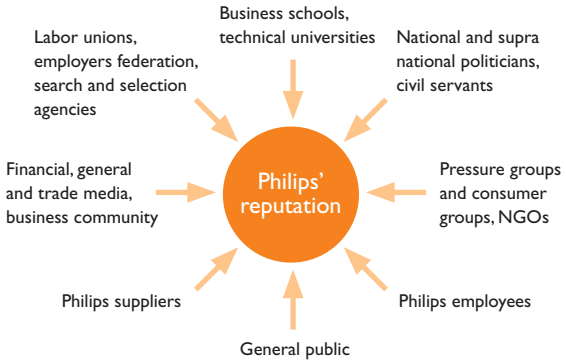
- New review and planning process
- Challenge & Connect leadership development workshops
- 'The Simplicity Event' for opinion leaders

Engaging

We are continuing to strengthen our approach to stakeholder dialogue, working to create more structure around stakeholder engagement and integrate stakeholder management into our business processes.

Taking action

Following up on our reputation study, which has been detailed in previous reports, we introduced a review and planning process for 40 key countries. This new process includes a review of existing and desired stakeholder relationships, local evaluation of key issues and a refreshed plan for 2006 to increase and improve stakeholder dialogue. Tools have been developed and deployed to facilitate this process, including a self-assessment tool for stakeholder mapping, a bottom-up issues management grid and a consistent stakeholder engagement planning document. The feedback is being analyzed and will result in improved programs.



Challenging ourselves

Twenty-five Challenge & Connect workshops were held in all four regions – Europe, North America, Latin America and Asia Pacific. Each workshop was facilitated by a member of the Group Management Committee. They encouraged an open, honest exchange of ideas and opinions, covering what our leaders need to do and how to work together as One Philips. The 1,400 senior managers who participated worked to:

- Define what One Philips leadership is in a way that is universally understood.
- Align with this strategy and deliver its key messages to their teams in meaningful and persuasive ways.
- Pinpoint challenges and commitments they need to make.
- Create an environment for change that inspires and energizes others.

Participants were given tools to support them in their own leadership development. They took a frank look at their competencies, shared their assessments with the group and defined what they need to do differently. Through the workshops, we've begun equipping our leaders to be bolder and more decisive, to promote greater creativity and engagement.

The Challenge & Connect workshops are part of a longer-term strategy to transform our company. And it isn't

with stakeholders

about the actions of senior managers alone. It's about leaders inspiring employees to get involved – to understand that One Philips is about mindset, ways of working and value creation. One example of employee involvement is the first-ever One Philips awards, created to recognize employees or teams whose work truly embraces One Philips. Employees were invited to vote for the winners of this prestigious internal recognition. The DISHA team won the gold award, illustrating our employees' interest in building business in new and emerging markets (see page 25).

Online dialogues for 2006

Picking up on feedback from our Challenge & Connect workshops, which called for more dialogue and involvement in company policy, we have initiated a series of global online dialogues for 2006 between senior management and employees.

Demonstrating the future, gathering feedback

In 2005 there was widespread stakeholder outreach related to the company's brand positioning "sense and simplicity". We held open presentations and meetings early in the year in 11 major markets where our brand campaign was being rolled out. We conducted sessions for key audiences including, media, marketing, customers and suppliers.

In September we held 'The Simplicity Event' in Paris for more than 1,000 international opinion leaders. We shared our vision of simplicity in the next three to five years as it affects our customers and end-users, as well as how it is being implemented in our company.

Philips Design and Philips Applied Technologies presented 18 concept products, demonstrating the future look and feel of simplicity-led design in healthcare, lifestyle and technology. A broad cross-section of attendees was interviewed for their feedback, which will be used to inform our future planning. This event was supported by our Simplicity Advisory Board, a cross-disciplinary team of experts from the worlds of architecture, fashion, IT, medicine and automotive design – demonstrating our commitment to outside-in thinking.

Following this success, plans for 2006 include a Simplicity Event in New York in April.

You will read about more examples of stakeholder engagement throughout this report.

Our customers

	Medical Systems	DAP	Consumer Electronics	Lighting	Semiconductors	Other activities
Consumers		●	●	●		
Specialized retailers	●	●	●	●		
General retailers and multiples	●	●	●	●		
Wholesalers	●	●	●	●		
Small and large businesses				●		
IT industry (PC and peripherals)			●		●	●
Consumer electronics industry					●	●
Telecommunications industry					●	
Building industry				●	●	
Governmental organizations	●			●		
Automotive industry				●	●	●
Other industries				●	●	●
Hospitals and clinics	●			●		

Highlights

- Innovations based on understanding end-users
- Follow up after purchase
- Training and education for customers

Meeting customer needs

We work to meet the needs of our diverse customer base, illustrated in the chart. Our innovative products are designed to enhance our consumers' lives by providing access to the benefits of technology at home and on the move. Our professional products and services offer advanced solutions to help businesses stay ahead, today and tomorrow.

We are focusing our activities on the interlocking domains of healthcare, lifestyle and technology. Understanding the needs of our customers is our starting point as we pursue innovation in every aspect of our business. We believe that fresh new ideas based on the combination of consumer insight and technology leadership are key to creating new opportunities for growth and value creation.

Consumers influence our product creation process

Consumer feedback is an intrinsic part of our product creation process and is a crucial part of building relevant value propositions for both our consumers and business-to-business customers.

Our approach to end-user insight generation and value proposition validation is becoming a standard way of thinking and working to create propositions based on real insights from the people who actually use our products. The objective is to capture outside-in thinking – from the point of view of the end-user – through a proprietary multi-step process used throughout the company. This ensures that our initiatives are new and meaningful innovations based on a true understanding of trends, market demands (what the end-user wants) and technology. It also helps us consistently deliver on our brand promise, "sense and simplicity".

Gathering consumer insights

How do we get consumer insights? We talk directly with end-users at 'Meet and greet' sessions and in-home visits. We discuss people's challenges, wishes, aspirations and potential solutions for those. We then evaluate those same insights and value propositions via qualitative interactive processes and Internet testing, where respondents evaluate insights and propositions quantitatively and qualitatively. We also collaborate with outside experts on a regular basis.

End-user insight generation and proposition validation process

Our consumer divisions invite end-users to our facilities. Domestic Appliances and Personal Care (DAP) has five consumer test centers around the world, in Drachten and Hoogeveen, the Netherlands; Klagenfurt, Austria; Snoqualmie, USA; and Singapore. Consumer Electronics (CE) conducts Consumer Experience Testing during the development phase in Experience Centers in Singapore, Hong Kong and Brugge, Belgium. Product validation testing to prove market readiness includes, among others, the ease of getting the product out of the box, time it takes to get it working and how easy it is to use the manual.

OEM (Original Equipment Manufacturer) customers are strongly involved in the specification design for innovations in Lighting and Semiconductors. During the product creation process, customer feedback is taken into account before passing any milestone. As in the consumer divisions, end-user insights are gathered and verified with key partners in the value chain. These insights are the starting point for product concepts, which are again validated before beginning the technical phases of the product creation process.

Our Medical Systems division uses the same process, taking the needs of its customers into account. This involves getting insights from physicians, technicians and patients. (See 'Listening to clinicians' on page 32.)

In this way, we co-create insights with end-users. DAP and CE, for example, are working on more than 100 new projects based on our insight generation process. It has proven to be highly effective, enabling us to create products that meet our end-users' needs and answer their desires, living up to our commitment to simplicity.

Understanding the trends

Philips Design supports the product creation process with an enriched approach to design that is research-based and focused on the end-user. This analysis includes the work of market researchers, psychologists, sociologists, philosophers and anthropologists to ensure we understand what consumers really want.

Connecting with people's lives

In the global Food & Beverage market, there are significant regional differences in culinary habits and the type of kitchen appliances used. In 2005, with a dedicated regional approach and a multidisciplinary team, we began preparing the launch of a range of rice cookers in Asia with the aim of becoming an active player in the highly competitive rice cooker market, dominated by local players.

What's the role of a rice cooker in an Asian family's life? That's what we were determined to find out. So we visited homes and talked to people about what matters to them when cooking this staple of the Asian diet.

Applying our end-user insight generation and proposition validation process helped us gather a great deal of information and select the insights end-users found most appealing. They want a way to cook nutritious meals quickly. Our high-quality rice cooker does just that, cooking rice fast and helping consumers save time. And the inner pot has a non-stick coating, to make cleaning fast and easy. But most important to Asian moms – the extra steam tray can be used for steaming different kinds of dishes in the healthiest way. This satisfies their need to provide their families with maximum nutritional value.

Like nothing you've seen before

The Ambient Experience is designed around patients and healthcare professionals. Based on extensive research – on how patients cope with undergoing a scan, how radiographers and clinical staff work, and the concerns of hospital administrators – the Ambient Experience responds to people's needs in a potentially frightening situation, by giving patients an exam environment they can control.

Drawing on expertise from across Philips – Design, Medical Systems, Lighting, Consumer Electronics and Semiconductors – the Ambient Experience creates a friendly, reassuring environment that puts patients at ease. With this significant quality of life benefit, the Ambient Experience is one of our innovative sustainable businesses.

The world's first Ambient Experience pediatric radiology suite opened at Advocate Lutheran General Children's Hospital in July 2005. This suite is designed to create a soothing environment that enables children to relax while undergoing computed tomography (CT) scans.

The Philips team worked collaboratively with pediatric radiologists, nurses, technologists, engineers, lighting designers, architects and a child psychologist to develop Philips Ambient Experience at Advocate Lutheran General Children's Hospital. The team studied each phase of a radiology examination – from waiting room and preparation to the scan itself – to design the suite around the needs of patients and clinicians. The result is an innovative radiology suite that improves the quality of care by easing young patients' fears and anxieties because they can select and control the room's lighting, sound and visual images.

Overcoming fear

The harsh reality of a radiology department can be overwhelming for children. A CT exam requires a patient to lie perfectly still, and can be very scary or intimidating to a child. Now 'cool' replaces 'scary' with our new imaging environment designed to engage young patients. It's a striking use of the latest advancements in ambient lighting, dynamic projection, radiofrequency technology and surround sound. With a Brilliance 40 slice CT scanner at its center.

Creating a sense of involvement

Kids like to be in control. And a sure way to release tension is to become part of the process.

From the moment they check-in to when they leave, pediatric patients make choices over the examination environment. The Ambient Experience allows young patients to:

- Choose a favorite animation from among six seen in the waiting room.
- Pick out a matching radiofrequency identification card that will activate the chosen animation in the scan suite.
- 'Scan' a toy in the nearby Philips 'kitten scanner' to get a child's perspective of the examination.
- Place their radiofrequency identification card on the big red 'X' when entering the scan suite to immediately activate lights, sound and images of the selected animation.

When it's time for the exam an animated character helps the child to hold his breath for the 20 seconds required to do the imaging study.

What does it all mean?

When the child is relaxed and comfortable in their environment, the need for sedation or repeat exams is reduced, which helps keep a young patient's radiation doses to a minimum.

Improved patient/family satisfaction creates a more positive environment with less anxiety, so the exam is therefore a more favorable experience for all involved.

At Philips we seek the sensible application of technology for the ultimate good of our customers and their patients. The Ambient Experience embodies that goal.

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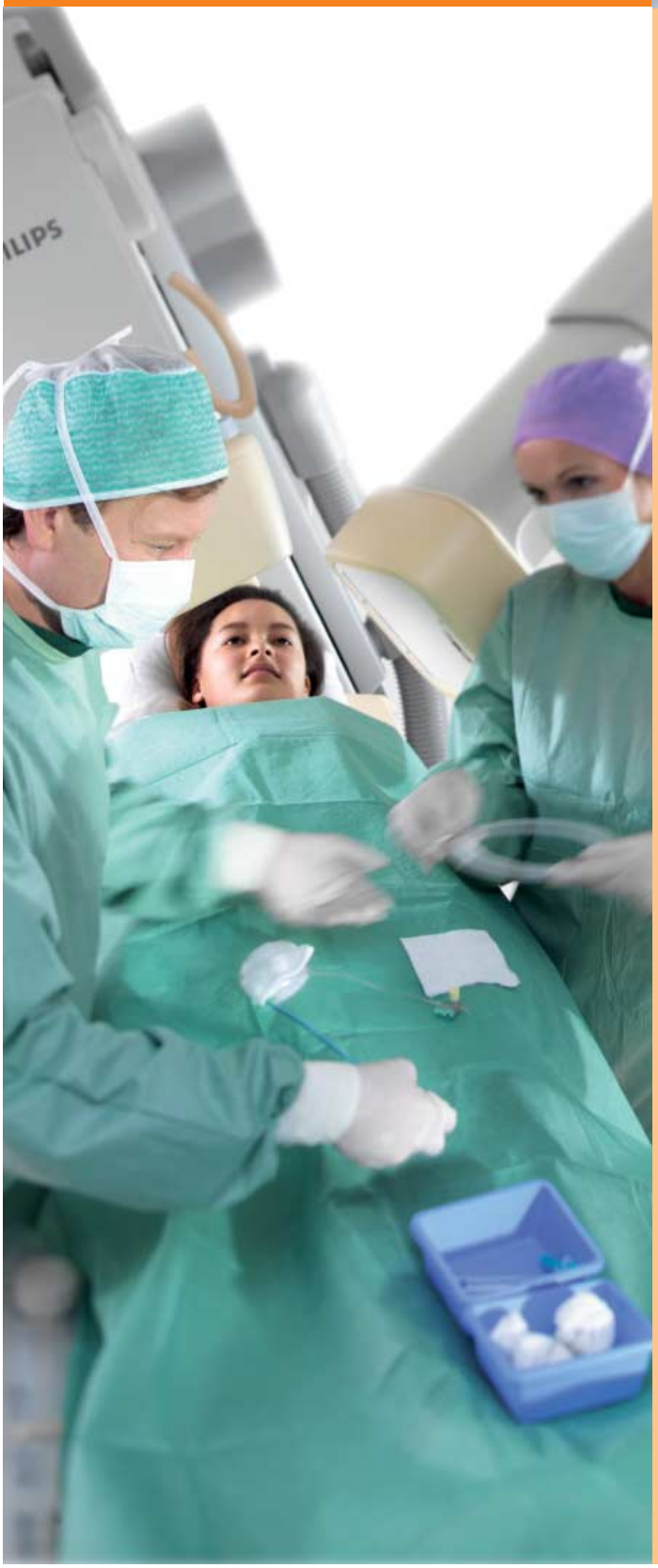
Listening to clinicians

Michael Söderman, M.D., Ph.D.
Department of Neuroradiology
Karolinska Hospital, Stockholm, Sweden



In September 2005 Philips announced robust, remote voice-control for equipment used in manually intensive or sterile medical situations. The voice-control system, known as Hands-free Interaction in the Hospital (HIH), can complement the clinician's way of working in situations such as diagnostics, catheter interventions or operations. Even when their hands are occupied, they need to interact with other medical equipment. HIH lets them do this by talking to that equipment from up to several meters away.

The convenience, reliability and accuracy of the voice control are proven to be promising in clinical trials executed at a catheter laboratory in the Department of Neuroradiology at Karolinska University Hospital in Stockholm, Sweden. Here the voice control was used in a prototype setting to select functionality and manipulate images on biplane neuroangiography equipment.

Dr. Michael Söderman discusses how this cooperative approach benefits all parties.

I have been collaborating extensively with Philips on several projects including the hands-free prototype. We get involved in clinical trials like this when we believe in the idea and there is a working prototype. This brings us added value because we can get access to hardware and software early and we can influence the final design of the finished product. At the same time, we know that we are in fact helping the company to improve its products.

I believe this process is critical for Philips because clinicians always use a system in ways that designers may never have imagined. What we do with a system is different – we have different working habits, are in a different environment and we have different ways of trying to optimize the equipment.

We provide information on what could be changed and improved – to optimize many things that are not perfect in the beginning – they cannot possibly be perfect at the outset. Getting the kind of input we can offer as a test site makes Philips better able to deliver useful products that benefit patients and clinicians.

Following up after purchase

We want information from consumers on every touch point – the moments when someone uses a Philips product, visits one of our websites, sees our products in a shop. For example, we invite consumers who purchase products from DAP and CE to become members of Club Philips, an online portal to a variety of content, services and product information. Consumers can go there to find the newest downloads and preview the latest innovations, music and games. Registered users are kept up to date on new software upgrades, or special content for their devices. They can also win prizes, and in the future will be able to test upcoming products. The Club Philips database will continue to develop as a platform for direct dialogue with the end-consumer. For example, we could e-mail consumers a targeted offer to purchase one of our products.

Philips Medical Systems tracks worldwide customer satisfaction on a quarterly basis by region and modality. This data is monitored and used by senior management to track our performance and determine opportunities for improvement.

For Lighting's top key accounts, which represent approximately 25% of divisional sales, the account plan is developed with the customer and agreements are included in a customer specific business balanced scorecard. This is monitored with the customer, resulting in corrective actions where necessary. For the remaining customers, satisfaction surveys are conducted on a rotating schedule on each continent, covering OEM and distribution channels. In these surveys our performance is compared with that of our main competitors on both product- and service-related topics. Corrective and/or structural improvement actions are defined on the basis of these results.

Handling complaints

Customer satisfaction and whether consumers will recommend Philips as a brand, is largely related to the experience with our products and services. To track that, we have a well-structured flow of feedback during the various stages of the lifecycle of our products.

To ensure dedicated follow-up on customer complaints or requests for information, we offer our consumers multiple ways to contact us:

- Our website offers downloads of user manuals, leaflets, product photos, frequently asked questions and more.
- Customer Contact Centers provide support by phone, e-mail, online chat, letters, etc.
- A network of external repair shops.

The Customer Service Group carries out research on a global scale to measure performance in these areas.

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Additionally, our consumer divisions have procedures to ensure that action is taken on consumer requests, problems or complaints, leading to further product or service improvements. This includes the work of our 'knowledge engineers' and marketing specialists, who carry out root cause analysis where consumers have expressed an insufficient level of satisfaction.

To handle technical product complaints, Lighting's order desks use the global Complaint Registration System, which provides a direct connection to the technical experts in manufacturing and response time is monitored as a critical performance indicator. All complaints are put into the SAP Quality Management Module, which is fully operational in Europe and will be rolled out globally. In addition to immediate corrective action at time of registration, the available statistics can be used for root cause analysis and structural improvement actions.

Customer education

We offer a variety of educational opportunities for our professional customers. Our Medical Systems division's educational offerings include an Online Learning Center; customized clinical user training focused on diagnostic and treatment; and specialized service training for biomedical engineers and other specialists maintaining Philips equipment.

Our Lighting Application Centers around the world provide hands-on opportunities for industry professionals to explore the fundamentals of lighting, real world lighting applications and the use of new lighting technologies.

Consumer Electronics has created the Philips Online Academy, an e-learning environment using online interactive multimedia courses, for its retailers. Training programs on our latest products and technologies are available in several local languages.

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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. We have developed a draft Philips Product Safety Policy to ensure a consistent approach that would also safeguard the need for customized divisional implementation as necessary. While we had expected to finalize and implement this draft policy in 2005, we have been unable to do so as there are still some issues to resolve.

Our employees

Touching lives every day

Through our products, Philips employees touch people's lives across the globe every day. As an employer we recruit talented individuals and touch their lives as well, by offering them inspirational experiences, rewarding teamwork, a company culture that values learning and inclusion, and the chance to stay in touch with products and technologies of the future.

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Measuring employee engagement

Employee engagement – how committed and motivated a person is in their job – is essential to our organizational effectiveness and a vital foundation for our continuing success. Measuring employee perception on the issues having the most impact on employee engagement helps us to build a working environment that fosters individual and company growth.

In 2005 we conducted employee engagement surveys for those businesses that did not survey employees in the previous year and follow-up surveys in many of the businesses that did measure engagement in 2004. A total of 124,015 employees were invited to participate in an

Highlights

- Employee engagement
- Diversity and inclusion
- Developing our people
- Health and safety

employee engagement survey. We achieved our target of an 80% response rate, a 5% increase compared with 2004.

We have developed indexes on specific topics, based on the results of a set of questions from our overall Employee Engagement Survey, to measure employee perception related to social aspects of organizational effectiveness. In our previous sustainability report we provided data on two indexes – Employee Engagement and Inclusion. In this chapter, we are reporting 2005 results for these indexes and are adding another, our Human Capital Development Index. You also will see the results of individual questions in other sections of this report. Because different parts of our company were surveyed in 2004 and 2005, these indexes are not yet comparable year to year.

Our product divisions and businesses held sessions where managers, employees and Human Resources discuss the outcomes of their employee engagement survey on a business, department or team level. Strengths and weaknesses are discussed and corrective actions are put in place to address areas of concern. We clearly communicate this information to employees via a variety of face-to-face, electronic and print methods.

We are focusing on making our Employee Engagement Survey a true One Philips survey that lives up to our commitment to simplicity. Beginning in 2006, our survey will be conducted annually on the same day around the world. Questions will be standardized and the number of questions will be reduced to make the survey simpler and comparable.

Employee Engagement Index

Based on three questions from the Employee Engagement Survey, our Employee Engagement Index allows us to report the level of employee engagement with a single figure.

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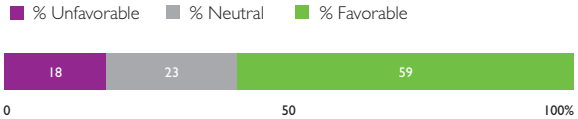
Employee Engagement Index



Source: Philips Employee Engagement Survey 2005
Number of responses: 100,646

Diversity and inclusion

Our vision is of one company made up of many different faces. We foster a working environment led by people who understand that diversity and inclusion (D&I) provide a competitive advantage.

To raise D&I awareness, we introduced two types of workshops in 2005:

- A half-day Inclusive Leadership Awareness Workshop for divisional/regional/functional management teams, which is being rolled out around the world.
- A one-day D&I Awareness Workshop for the rest of the organization, which is being rolled out in Asia and will be piloted in other regions in 2006.

We also launched the Reciprocal Mentoring Program, which was piloted with four teams comprised of senior management members and top potentials. With its unique 'two-way street' approach, both the senior and junior participants can learn from each other and broaden their frames of reference.

Our diversity and inclusion intranet site, providing internal information as well as external best practices, was launched in April 2005. The D&I message was also embedded into various processes including the Philips Career Center on the Internet and In Touch, our introduction program for all new employees.

Diversity and inclusion task forces

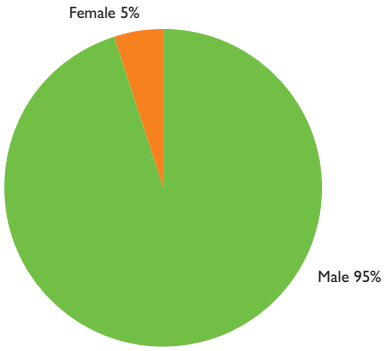
A network of more than 30 champions from all businesses and regions is now firmly established. Within this network four Champion Task Forces have been working on specific topics, including the establishment of D&I Awareness Workshops for mid-level employees; reviewing hiring processes; and looking into management development processes to identify – and help eliminate – any possible biases. In 2006 the network will become more regionally focused, to address region-specific issues.

Affinity networks

Wynergy, our network for women executives, aims to create a balanced environment that facilitates the personal success of all women at Philips. We believe this puts them in a better position to influence cultural change within the organization. Other affinity networks for women are being established in different regions.

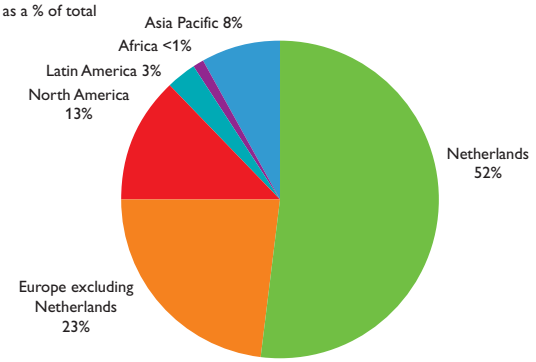
Composition of Philips executives (total = 778) at year-end 2005

as a % of total



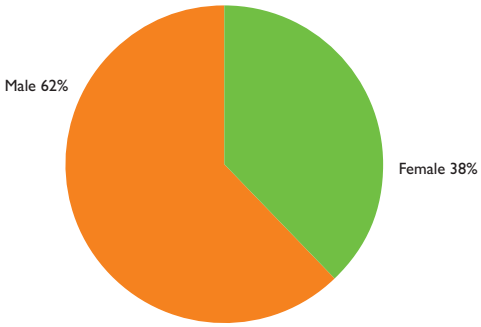
Regional origin of Philips executives at year-end 2005

as a % of total



Employees by gender at year-end 2005

as a % of total



We are working to increase opportunities for women and other under-represented groups in key positions, and are focusing on developing a diverse talent pipeline. We believe we have a firm foundation to help us reach our goals:

- We want to increase the percentage of women in senior management and executive positions to at least 10 percent within four to five years, more than doubling our level of 4% in 2002. While the number of female executives increased to 37 in 2005, the percentage remained stable at 5%. The percentage of women in the top potential pool was 11% at year end.
- We want to increase the percentage of non-Dutch nationals in key executive positions. The percentage of Asian executives was up to 8% in 2005, from 7% in 2004. The percentage of Asian top potentials increased to 13% from 12% in 2004.

Through our products, Philips employees touch people's lives across the globe every day.

Inclusion Index

To refine our Inclusion Index, in 2005 we developed a cluster of 11 questions, which were added to our Employee Engagement Survey. The previous Inclusion Index was based on four questions from the 2004 survey.

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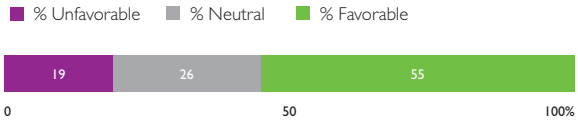
Inclusion Index



Source: Philips Employee Engagement Survey 2005
Number of responses: 100,646

Developing our people

'Develop people' is one of our company values. We take a blended approach to learning and development, offering a wide range of opportunities to meet individual learning styles and needs. Employees can select from classroom training, web-enabled learning, built-in assessment and after-activity follow-up.

In 2005, 11,000 employees participated in programs in the Core Curriculum, achieving our target of more than doubling the 2004 participant number. Our Core Curriculum offers learning opportunities in the areas of personal effectiveness, working together and people management.

We launched three Functional Core Curricula, addressing the functional areas of Marketing and Key Account Management/Sales. In total 1,600 employees participated in these programs during the launch phase.

We expect to continue with a similar level of participation in the Core Curriculum programs, with a significant increase in participation in the Functional Core Curricula. Our activities in 2006 will include continuing to improve the quality of programs offered in each of the regions, as well as adding programs and new curricula, including Human Resources and IT.

To measure our employees' opinion of their development opportunities, we established a Human Capital Development Index (HCDI). With this report, we can begin providing information on our HCDI, which is based on three questions from our Employee Engagement Survey.

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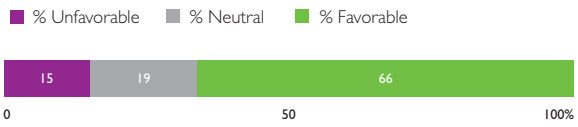
Human Capital Development Index



Source: Philips Employee Engagement Survey 2005
Number of responses: 100,646

Creating the best place to work

Tjerk Hooghiemstra
Global Head of Human Resources
Member of the Sustainability Board

A key element of sustainability is to be a good and responsible employer. At Philips we work hard to be much more than that. We want to be the best place for people to work. We want to create a working environment that challenges, energizes and engages people. That is a workplace where people are respected, whatever their nationality, gender, cultural background, profession or other characteristic.

I would even go a step further. We want to be a place characterized by curiosity about differences because we are convinced that creativity – the fuel to our success – springs from people looking at things from different angles.

Are we there already? To an extent, but there is still more work to do. Over the previous years we have worked to provide people with excellent development opportunities. We have for instance put in place People Performance Management (PPM), Development Centers and Core Curricula to help people identify their development needs and find opportunities to learn.

Leadership

Feedback from our Employee Engagement Surveys shows that in general our leaders need to improve on supporting and coaching their people. Hence we are putting a lot of effort into leadership development. One example is our Challenge & Connect workshops, which are discussed on page 26.

We have redefined the Philips Leadership Competencies to more strongly reflect the people side of leadership, as well our One Philips spirit. But in the end it's every leader's responsibility to embrace the idea of being a great people leader and act accordingly.

Diversity and inclusion

Being creative and in touch with our end-users is the foundation to our success. What better way to achieve this than to ensure that we are a reflection of the outside world. The more curiosity about differences in cultural values, professional backgrounds, ways of thinking, life preferences, personal motives, the richer our corporate culture.

Touch lives every day

We improve people's lives through our products. In doing so, we touch the lives of people every day. Through the light bulbs that light their home, the mobile phones that connect them to their loved ones or through an ultrasound image that shows their unborn child. That's why 'Touch lives every day' is our employee value proposition. We get excited to do just that and when we recruit we look for people who are thrilled to join our journey.

Responsible transformation

The taskforce on Responsible Transformation continued to review practices regarding transformation issues in Europe, evaluating the position paper 'Responsible Transformation within Europe'. We will continue to act responsibly, safeguarding the interests of employees, and will accelerate efforts to improve employability to ensure that employees are equipped to change jobs, either within or outside the company, quickly and smoothly.

To learn from previous restructuring experiences, the EPF intranet site provides key statements from the position paper and a 'Checklist for Responsible Transformation'. This checklist is as guide to help facilitate meaningful dialogue between local management and employee representatives. It also helps to evaluate the transformation process after completion.

Health and safety

Philips aims to maintain work environments that are free from all risks and hazards to the safety and health of our employees. To drive improvement, we track our performance via Key Performance Indicators.

Health and safety performance

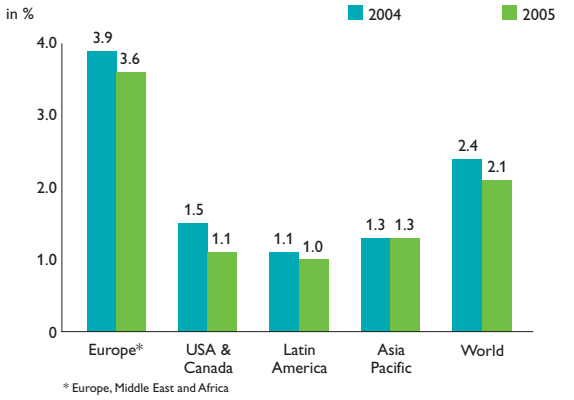
We have made further progress in implementing our program for standardized data collection and reporting of health and safety data throughout the company. As part of our ongoing efforts to improve the quality of data, we conducted training, as well as internal audits at various facilities around the world. In addition, our external assurance provider has assessed the robustness of our data collection systems at 12 of our sites, and the results will be used for further improvement.

In 2005, the reported data covered 88% of all Philips employees in terms of FTEs (full-time equivalents). This coverage is slightly lower than in 2004. This is mainly attributable to reporting in the Netherlands where a change to reporting at product division level caused a temporary setback as reporting had to be organized within each division.

Lost Work Time

The Lost Work Time rate decreased in 2005 to 2.1% of the contractual working hours lost due to sick leave, compared with 2.4% in 2004. Approximately 3% of this was caused by occupational illness and injuries. Levels of absenteeism differ per region because they are largely dependent on cultural factors, as well as different applicable legal and contractual compensation systems. In all regions absence levels were relatively stable over the four quarters of the year.

Lost Work Time rate



Lost Workday Injuries

In 2005, we recorded 954 occupational injury cases causing the injured employee to be unable to work the day after the injury (Lost Workday Injuries). In 2004, 1,070 Lost Workday Injuries were reported. For the Philips Group there were 6.9 Lost Workday Injuries per 1,000 employees in 2005, down from 7.2 in 2004. We consider this level of injuries to be too high. Therefore, we are committed to further reduce Lost Workday Injuries in 2006.

Our Lighting product division reported 53% of all Lost Workday Injuries in 2005. These injuries can typically be associated with working with lamp glass, manual loading and unloading of machines, and working with high-speed machines during normal operation (e.g. flames and hot surfaces) or during a maintenance period. We strive to investigate the cause of injuries and take steps to prevent reoccurrences.

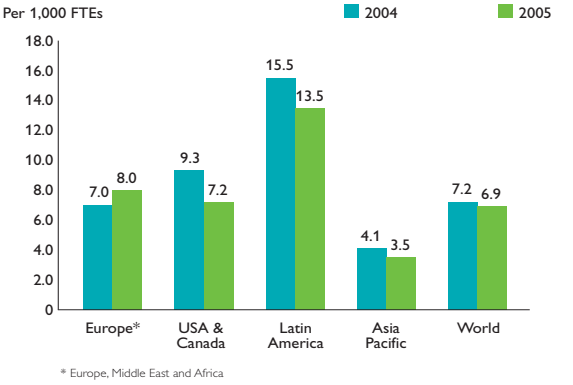
Caring for employees and their families

Philips Lighting in Monterrey, Mexico, has had a full-time doctor on staff for employees since 2002. Nurses provide care when the doctor is not on duty, and he is available to return to the site as necessary.

In November 2005 medical care was extended to employees' families, beginning with flu vaccines and dental care. Nearly 11,000 employees and family members were treated during the year.

To further enhance employee safety and well-being, the plant initiated the STAR program (Safety in Work Alert to the Risk). To prevent accidents workers report unsafe conditions and practices. Through this program we have detected 172 unsafe conditions. More than 60% have been resolved, with the remainder in progress.

Lost Workday Injuries



No occupational fatalities were reported in 2005, and no major incidents occurred resulting in severe injuries.

Improving our reporting system

We recognize that the quality of our health and safety data needs to be improved through a better understanding of the standard definitions by our reporting organizations, and through internal control procedures. We initiated actions to further improve the quality of reporting in 2005, and will continue this work in 2006.

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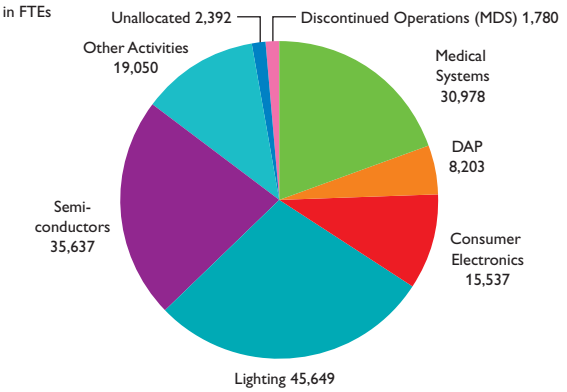
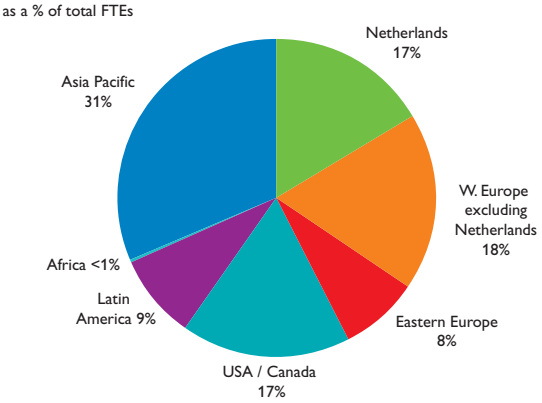
Our employees

The number of Philips employees at year-end 2005 totaled 159,226. This includes 1,780 employees belonging to the Discontinued Operations of Mobile Display Systems (MDS).

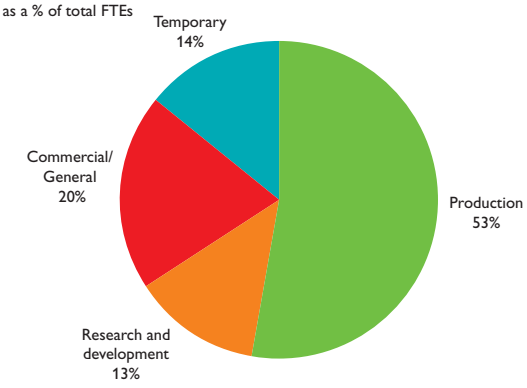
Employees per sector at year-end 2005



Employees by geographic area at year-end 2005

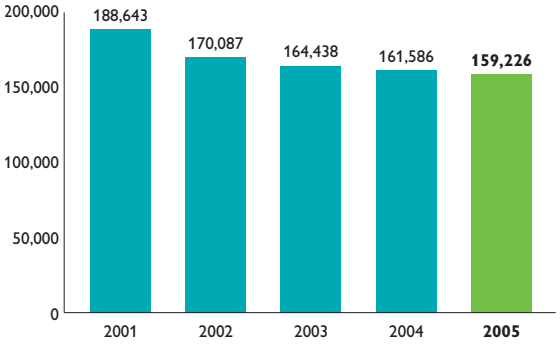


Employees by functional area at year-end 2005



Changes in employment structure

Employees (FTEs)



The number of employees decreased by 2,360 employees during the course of 2005. Changes in the portfolio resulted in a decrease of 757 employees on balance. Various deconsolidations caused a decrease of 2,552 employees, which was partly offset by the addition of 1,795 new employees from new consolidations, mainly related to the consolidation of Philips Lumileds Lighting US. The most important deconsolidations were:

- Various divestments of the previous ETG group (part of Other Activities), involving a decrease of 653 employees in total.
- The divestment of Philips OEM Monitors to TPV in China and Taiwan, involving a decrease of 1,469 employees in total.

Excluding these changes in the consolidated portfolio, the total number of employees decreased by 1,603, reflecting further outsourcing and the ongoing drive for efficiency. The most significant reductions occurred in the sector Other Activities, which were partly offset by a strong increase in Semiconductors.

Employment changes in 2005 by sector

in FTEs	position end 2005	portfolio changes	comparable changes
Medical Systems	30,978	0	133
DAP	8,203	0	7
Consumer Electronics	15,537	(1,469)	(106)
Lighting	45,649	1,795	(114)
Semiconductors	35,637	(15)	986
Other Activities	19,050	(907)	(1,759)
Unallocated	2,392	(161)	6
Discontinued Operations (MDS)	1,780	0	(756)
Philips Group	159,226	(757)	(1,603)

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

Employment changes in 2005 by geography

in FTEs	position end 2005	portfolio changes	comparable changes
Netherlands	26,110	(344)	(318)
W. Europe excl. Netherlands	29,145	(359)	(921)
Eastern Europe	12,787	0	742
USA/Canada	27,175	1783	(1,792)
Latin America	13,702	(76)	(266)
Africa	406	0	(5)
Asia Pacific	49,901	(1,761)	957
Philips Group	159,226	(757)	(1,603)

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 2005 by function

in FTEs	position end 2005	portfolio changes	comparable changes
Production	83,720	(660)	(2,061)
Research & development	20,300	(49)	(53)
Commercial/General	32,526	(12)	8
Temporary	22,680	(36)	503
Philips Group	159,226	(757)	(1,603)

Our role in the

Highlights

- Helping children with HIV
- Relamping rural schools
- Something to smile about
- Taking health to heart
- Encouraging children to ‘soar’

Focusing on health and education

With our targeted approach to social investment, we focus on improving health and education, particularly for the underprivileged, in the communities where we live and work. By linking initiatives with the scope of our business, we can make the most of our core competencies to make a difference in people’s lives.

In 2005 we launched a social investment database to gather information about the projects underway in our product divisions and country organizations. Our annual budget to support our projects totals EUR 9 million.

The year will long be remembered for monumental natural disasters, including the Indian Ocean tsunami, Hurricane Katrina and the South Asian earthquake. We moved quickly in the aftermath of these disasters, not only with financial support but also by sharing our expertise.

Our employees around the world joined the global relief efforts, volunteering their time and organizing fund-raisers. Volunteering time to train local medical teams or install equipment, Philips employees worked to help restore healthcare in the affected areas from Sri Lanka to Mississippi.

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community

Helping children with HIV

Fewer than 5% of HIV-positive children receive treatment and millions of children who have lost parents to the disease go without support, according to UNICEF and UNAIDS. UNICEF says that children are the "missing face" of AIDS, lacking access to even the most basic care and prevention services.

To help children affected by the disease in Manaus, Brazil, the Support Association for Children with HIV (Associação de Apoio à Criança com HIV) established Life House (Casa Vhida). While children with HIV get most of their medicines from the Brazilian government, medicine without proper care and nutrition is often not effective. As nutritional food helps HIV-positive people stay healthier and productive longer, Casa Vhida's nutritionist develops a food plan for each of the children.

Keeping families together

The non-governmental organization's (NGO's) mission is to provide children living below the poverty level with a temporary home where they can receive medical, dental and psychological support. Residents can attend school and participate in sports. And the facility also helps keep families together by providing assistance to siblings whether they have HIV or not.

Philips employees have worked with Casa Vhida since the year 2000. To support the NGO's focus on proper nutrition, we conduct an annual food drive. Employee contributions and the company's matching donation reached a total of 8 tons of food in 2005.

Philips employees frequently spend time with the children, playing games and musical instruments, swimming, giving environmental classes and organizing barbecues. A group of line operators from our site in Manaus perform plays on special events, including holidays and the children's birthdays. The goal is to allow them to have a childhood.

This spirit of volunteerism starts at the top, with the plant manager who serves as treasurer on the Casa Vhida board of directors.

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Relamping rural schools

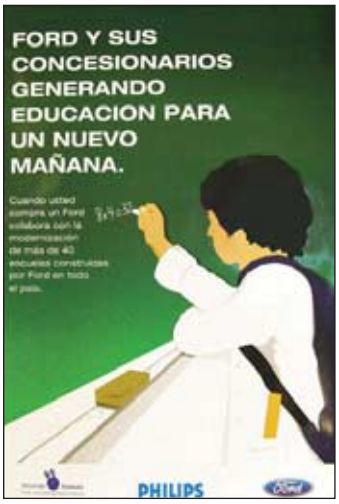
While Argentina's economy began recovering in 2003 after the social and economic crisis in 2002, the country

still faces challenges reducing social inequality in the rural sector. According to the World Bank, "The education system in Argentina has had a rich history in rural areas, but it still faces pockets of low coverage … and the quality of education for all regions across the nation can benefit a lot from renewed policy attention towards the rural sector."

To address this issue, we established a partnership with Ford Motors Argentina in 2003 to help modernize rural schools that Ford built between 1967 and 1982. Building on our knowledge that correct lighting systems stimulate learning, we are working to relamp rural schools to help improve the quality of education for underprivileged children.

The professionals in our Lighting Application Center volunteer to develop a customized plan for each school. We then donate the necessary lamps, providing the schools with the latest energy-saving environmentally sound technology.

So far seven schools, each averaging about 40 students, have been relamped thanks to our support. We will continue to work with Ford in 2006 to relamp four more schools in underdeveloped parts of Argentina.



Through our partnership with Ford Motors we help modernize rural schools in Argentina.

Something to smile about

Music and entertainment have long been known to help healing. Due to lack of funds, many healthcare facilities do not have play or rest areas for young patients. To make a child's stay in a hospital easier and more beneficial, in 2002 we launched our Smile Campaign in the Middle East to refurbish playrooms in healthcare facilities.

Philips employees help select the institutions and develop the renovation plans. Our employees do the work themselves, installing electronic equipment including TVs, DVDs and stereos at the facilities.

We're educating people in mountainous Eastern Taiwan about preventing periodontal disease, a main contributor to heart disease and diabetes.

In 2005, 700 children benefited during their stays in one of the facilities we worked with – an autism center, a home for special needs children and four hospitals.

Taking health to heart

Heart disease and diabetes are two of the top-10 causes of death in Eastern Taiwan. This part of Taiwan is largely mountainous and densely forested, making its populated areas difficult to reach. As a result, the standard of living there is generally lower. People are often poorly educated and less aware of healthcare issues.

Domestic Appliances and Personal Care Taiwan is doing something about this by launching Naruwan, a four-year educational campaign with the theme 'We care for your health'. Research has shown that periodontal disease is one of the main contributors to heart disease and diabetes. So Naruwan – translated "How are you?" in aboriginal Taiwanese – focuses on improving oral health.

We kicked off the Naruwan campaign in May 2005 in Hua-Lien County, where we saw the most serious consequences of poor oral health. A press conference with the Government Departments of Health and Education was followed by a series of 15 seminars on preventing periodontal disease, attended by some 650 people in 13 districts.

In August, we supported the Hua-Lien Health Bureau in training 105 primary school nurses on teeth cleaning for children. The campaign also includes a three-generational teeth-cleaning contest and painting competition for school children.

Encouraging children to 'soar'

Philips South Africa has consolidated all of its healthcare and education initiatives to ensure maximum impact and truly make a difference in the lives of underprivileged children. So far, more than 5,000 students have benefited from this focused program known as Project SOAR – Supply Opportunities and Achieve Results. Our customers and suppliers are also actively involved and have provided goods and services to Project SOAR at cost or for free.

During the past three years seven schools have undergone renovations including electrical upgrades, bathroom repairs and improved security. Philips employees can often be found on their hands and knees scrubbing floors, painting walls and planting trees at the schools. In addition, the principals of these schools prepared wish lists, which saw libraries, soccer fields, covered assembly areas and even gardens established through SOAR.

We continued this work in 2005, and also began working directly on educating the children through a variety of activities, including educational trips and events. For example, students saw a wide variety of exhibits at the Sci-Bono Discovery Centre, one of the largest science venues in Africa. Many of the schools in our SOAR project do not have the equipment for science experiments, so Sci-Bono is a good place to see the practical side of the science, math and biology curricula.

Empowering young girls

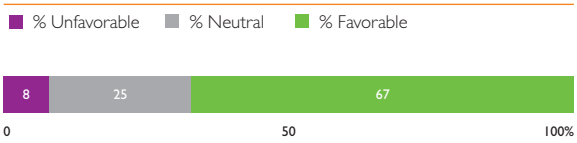
While women represent nearly 52% of South Africa's population, only 30% contribute to the country's total income. Girl children often face significant socio-cultural barriers at an early age and this is further aggravated by poverty and a lack of financial resources.

To help change this, we participate in 'Take a Girl Child to Work Day', South Africa's well-known and collaborative initiative focused on girls. This program sees thousands of girls between the ages of 14 and 18 accompany an adult to work. The objectives are to break down gender stereotypes that prevent many young girls from realizing that they have a right to work and equip themselves with qualifications for demanding or high-paying careers traditionally considered male domains. The project also aims to promote awareness of gender issues among boys.

We hosted 20 girls for the 2005 event. They visited Domestic Appliances and Personal Care, toured Consumer Services, enjoyed demonstrations of our Medical Systems' equipment and ended the day with a team building exercise.

In 2006, SOAR is expanding its horizons with investments in two health clinics, as well as additional educational activities.

Employees' response to:
'Philips is socially responsible in the community'



Source: Philips Employee Engagement Survey 2005
Number of responses: 93,991

With Project SOAR in South Africa, we 'supply opportunities and students achieve results'.

Our environmental

Highlights

- More than 160 Green Flagship products on the market
- 34 new Green Flagships with improved energy efficiency
- EcoVision II results
- Take-back and recycling evolves

Key global challenges

In our *Sustainability Report 2004* we discussed key global challenges. In terms of the environment, we believe the 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.

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Climate change

Attention on global warming is increasing, with the severe weather and natural disasters that occurred around the world during 2005. Indeed many scientists agree that higher temperatures are causing more powerful storms and perhaps intensifying extreme weather events, ranging from drought and wild fires to ice storms.

The United Nations Climate Change Conference 2005 held in Montreal, Canada, was the largest meeting of its kind since the Kyoto Climate Conference in 1997. It closed on December 9, 2005 with the adoption of more than 40 decisions to strengthen global efforts to fight climate change.

At Philips, we work to improve the environmental performance of our production activities and our products.

performance

Our production activities contribute to CO_2 emissions directly through the use of fossil fuels and emissions of chemical substances like Per Fluorinated Compounds (PFCs) in our Semiconductors division, for example; and indirectly through the use of electricity.

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To reduce this impact we have made the reduction of energy consumption in manufacturing, and the resulting decrease in the emission of global warming gases, a priority at Philips since the early 1980s. This was continued in EcoVision II, our environmental action program that ran from 2002-2005. Our results can be found on page 52.

Consumers contribute to global warming by using electrical and electronic equipment. Reducing the power consumption of our products has been one of the main focal areas in our EcoDesign activities we started in 1994. The aim is to offer products with superior environmental performance, including minimal energy use in standby mode or lower energy consumption during use, compared with predecessor products or commercial competitors. This lowers the cost of use for the consumer and has a positive effect on the environment. Examples of our top EcoDesigned products are highlighted on pages 54-57.

Directive for environmentally sound design of energy-using products

The EU Directive on the eco-design of energy-using products – known as EuP – aims at improving the environmental performance of products throughout their life-cycle by systematic integration of environmental aspects at the earliest stage of their design. With our industry partners, Philips took a leadership role in helping shape this legislation to ensure a well-balanced approach in which both industry competitiveness and the environment would be properly served.

A single set of EU-wide rules for eco-design will ensure the free circulation of goods in the EU internal market. This coherence also prevents potentially higher environmental impact caused by manufacturers having to design, produce and transport product variations.

Philips welcomes this Directive as an important element of efforts to promote greater use of more energy efficient products and to reach the goals set by the Kyoto Protocol. We have long viewed environmental improvement as an opportunity for innovation and believe that with EuP we can use our in-house skills to take our EcoDesign activities to a higher level.

Reducing energy and CO_2 emissions with our latest lighting systems

Theo van Deursen
CEO
Philips Lighting

In 2005 we launched an awareness raising initiative to highlight the untapped environmental and financial potential of new energy efficient lighting systems, which are available on the market now. Through this initiative, we are providing information to European municipalities and companies on how they can save millions of euros on energy costs and substantially reduce CO_2 emissions through lighting.

Figures show that if all energy inefficient lighting in Europe were upgraded to the latest technology solutions – for domestic, public and private sectors – the annual running cost savings would be more than EUR 4.3 billion, equivalent to CO_2 savings of 28 million tons per year. This equates to more than 50 million barrels of oil per year or is the equivalent CO_2 consumption of nearly 1 billion trees.

New energy efficient lighting technologies provide a unique win/win/win opportunity:

- The environment gains because of less CO_2 emissions.
- The taxpayer and user gain because of lower energy cost.
- European competitiveness is enhanced with its consequences for jobs, investment and exports.

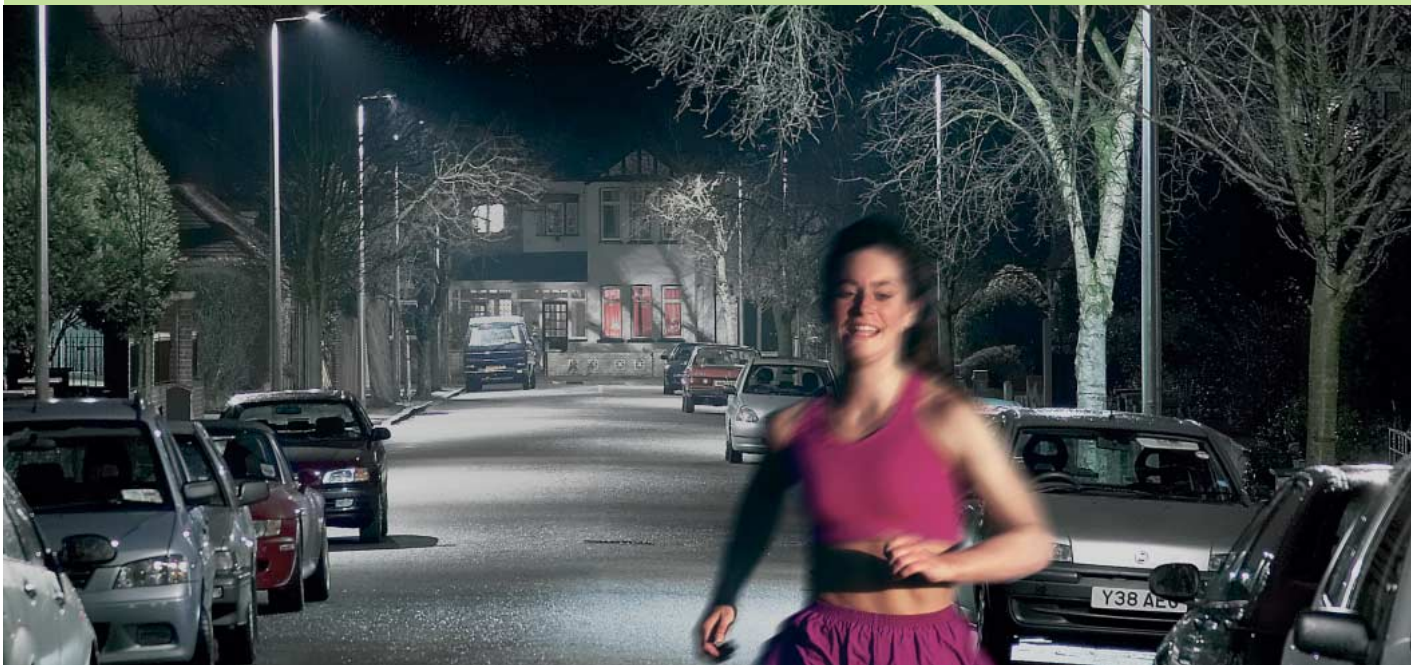
Both municipalities, financial institutions and political leaders have an important role to play in actively encouraging, promoting and engaging Europe to accelerate the adoption of these energy saving and CO_2 reducing technologies.

Of course there are very many places where this is already happening. Take for example the City of Gent in Belgium which won the 2004 International City People Light award for its new lighting design using energy efficient lighting technologies. However the current rate of market change is slow. Approximately half to two thirds of all Europe's lighting is still older energy inefficient technology, which at current rates will take another generation to replace. And this is despite the fact that quick financial paybacks are demonstrable.

We have invested approximately EUR 400 million in "green" lighting technology during the last five years.

Let's take a look at just one of our new products – Philips CosmoPolis street lighting systems, one of our Green Flagship products. More than twice as efficient to run as older mercury vapour lamps, CosmoPolis systems contain industry leading low levels of mercury and provide a significantly better quality of light.

Given the obvious need for lighting on our roads, we believe we should look to use the most efficient lighting available. That's why we're calling for more action to replace inefficient lighting in Europe, and are working to create awareness about the issues and explain the solutions.



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.

'Restriction of Hazardous Substances'

The European Union's Directive on the restriction of the use of certain hazardous substances in electrical and electronic equipment, commonly known as RoHS, will ban the placing on the EU market of new electrical and electronic equipment containing more than the agreed levels of the heavy metals cadmium, lead, mercury, hexavalent chromium and flame retardants poly brominated Biphenyls (PBB) and some poly brominated biphenyl ethers (PBDE).

In 1998 Philips began proactively restricting the use of cadmium, mercury and PBBs/PBDEs in many product categories. The main concern was lead, and to a lesser extent chromium, which needed to be phased out to comply with the new legislation, which goes into effect on July 1, 2006.

Our global policy applies the RoHS requirements to all of the markets we serve. While medical equipment is currently not in the scope of the RoHS legislation, our Medical Systems division is proactively eliminating these substances where possible.

RoHS implementation challenges

For the last 80 years lead has been widely used in electronics for soldering and other applications, like glass and phosphors in lighting, for example. Given the variety of our product portfolio and the many applications of this substance, eliminating lead from our products has proven to be a major operation that took many years. We worked to find cost-effective, commercially available and reliable solutions that would not compromise product quality and performance. Where no technically viable alternatives could be found, we worked with relevant trade associations to obtain exemptions to the RoHS directive.

We developed new manufacturing processes and carried out numerous reliability tests. Our product designs were adapted to the difficult technical conditions of lead-free soldering and RoHS compliant materials. Philips is also a leading company in developing applicable testing standards for RoHS compliance.

A new look at 'old' products

With the Philips Diamond Select program healthcare providers can choose a select group of our most reliable pre-owned systems, which have been carefully selected, refurbished, updated and rigorously tested. This sustainable business model:

- Makes optimal use of resources by refurbishing pre-owned equipment.
- Improves patients' quality of life by making highly reliable medical equipment available at lower costs. Having Diamond Select as an option, many healthcare providers have been able to solve serious problems without compromising their standards for clinical excellence and patient care.
- Is a growing business within Medical Systems, offering solutions for pre-owned equipment that keep residual values high and grow the customer base.

The driving goal behind our Diamond Select Program is to make first-rate equipment available for lesser cost – using only the best maintained 'new' systems, refurbishing all components, renewing all vacuum parts and offering full warranty and service contracts. As our customers have found, not all applications require new equipment, and Diamond Select affords greater flexibility for facilities looking to extend their resources and maintain clinical excellence and patient service, while building efficiencies for clinicians and staff.

In addition, we treat our refurbished systems like new. This is far from "as is" equipment that is deposited at the loading bay. Our systems are carefully delivered on time and installed with the same precision applied to brand new machines.

In terms of supply chain management, we had to ensure that tens of thousands of components and materials were RoHS compliant and that old and new components were not mixed up in the logistic processes. Various IT applications needed alteration to handle new design, logistic and distribution requirements. In addition to internal planning, we have actively trained suppliers on how to adhere to the RoHS requirements. (See page 70.)

Take-back and recycling

The EU Directive on waste electrical and electronic equipment (WEEE) makes producers responsible for taking back and recycling electrical and electronic equipment. Unlike EuP, legislation related to WEEE varies by country and some countries have not yet put legal requirements in place. As a result, implementation is complex.

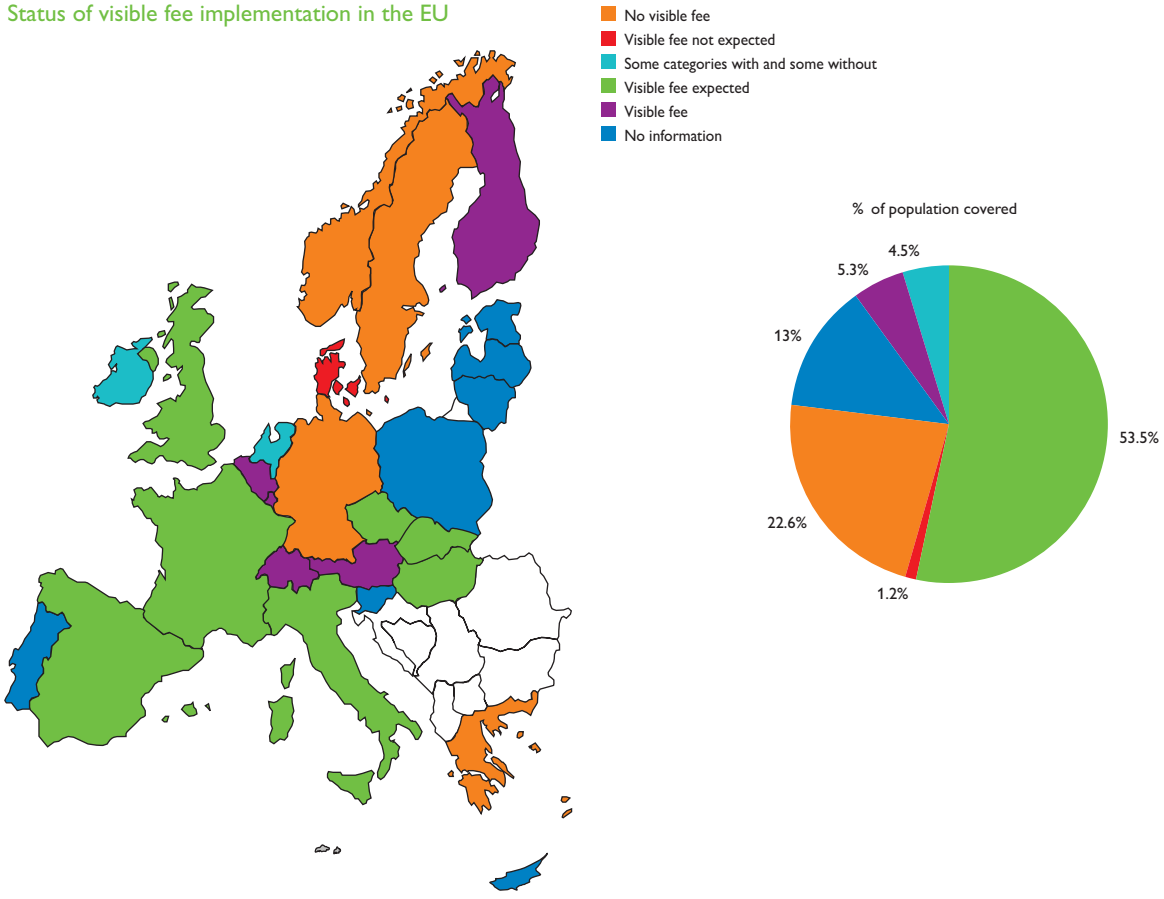
Electronic and small electrical products contain only fractions of materials that have any value on the market for secondary raw materials. The challenge is to balance this with the substantial costs of logistics and labor for disassembly and recycling.

Our approach is to cooperate with competitors to organize logistics and select certified recycling companies. This is realized by setting up collective take-back systems in the individual member states. We also favor the visible fee for take-back and recycling, which consumers pay at time of purchase. This creates transparency and consumer awareness. It's about creating systems that will work for all concerned.

Many European countries have adopted or plan to adopt the visible fee, as illustrated below. Experience in Belgium and the Netherlands over the past years proves that this approach works. In the Netherlands, for example, the collection rate increased in the early years and has since stabilized, while costs have decreased. A visible recycling fee is also used in California, USA, where it is already leading to a significant amount of recycled produts in its first year.

Legislation concerning the take-back and recycling of electrical and electronic equipment is being shaped in other US states and in China, as well as other countries.

Status of visible fee implementation in the EU



Philips sets high standards with EcoVision

Klaus Toepfer
Executive Director of the United Nations Environment Programme (UNEP)

The wasteful use of our resources – from energy, chemicals and wildlife to our land, air, rivers and seas – translates into a wasted environment, wasted lives and wasted opportunities for sustainable growth in both developed and developing countries.

Unless we can dramatically reduce waste in all its forms and better husband the planet's natural resources, we will kill the very life support systems of the planet upon which we all intimately rely. We will also find it nearly impossible to achieve the internationally agreed Millennium Development Goals by 2015. The goals cover poverty eradication and reducing hunger; better prospects for women and children; and reducing the spread of old and new diseases.

The Johannesburg Plan of Implementation, agreed at the World Summit on Sustainable Development in 2002, is an important blueprint for action. It includes this over-arching issue that cuts across all others: "The 10-year framework of programs in support of regional and national initiatives to accelerate the shift towards sustainable consumption and production."

Whether it be heavy metals like mercury, cleaner and greener energy schemes, better management of water resources, of forests, of animals – you name it – the 10-year framework touches all areas.

In Europe we once talked of the Cradle to Grave policy, but that is no longer enough. There must be life beyond the grave. So Europe has pushed forward producer responsibility backed up with measures including 'take-back' schemes.

Johannesburg gave us the Life Cycle Economy. China is pioneering the Circular Economy. Meanwhile Japan has developed the 3R's of Reduce, Re-use and Recycle. Maybe we should add a fourth R. Repair.

The target of all these approaches is greater efficiency and a revolution in resource management. If waste must arise, it must be minimized in quantity and toxicity, and it should be given value. It should be seen and used as a raw material – not something to dump or throw away.

So we have different approaches. But all rivers flowing into the same sea.

It is incumbent on elected governments to set the mood music, to create the legal framework and guidelines within which society operates. But it is also incumbent on socially responsible corporations to meet these requirements and, in my opinion, to go further. This is in their own self-interest not least in a world with oil pushing $70 a barrel and never ever likely to return to the luxurious low levels of the past.

It is also in the self-interest of industry to adopt creative and forward looking policies on resource efficiency because consumers are demanding goods and services that have an ever-diminishing environmental footprint.

Studies also indicate that companies that adopt wide ranging and continuous and searching reviews of their operations in order to meet corporate social and environmental responsibilities are more efficiently run and ultimately more profitable. A fact that I believe will be increasingly reflected in the share price and thus a company's ability to raise money on the capital markets.

So I applaud Philips' EcoVision program as a concrete contribution to greater resource efficiency, to greater worker and social health and to helping to achieve wider environmental gains.

It, alongside other corporate examples, sets high standards that I sincerely hope other parts of the electronics industry and industrial sectors within the developed and rapidly developing world will take on board.

If we are to win the battle for sustainable development, if we are to meet the genuine aspirations of all of the more than 6 billion people on this wonderful planet Earth, we must be creative and constantly in search of solutions.

The students of the genius Albert Einstein once asked him why he was asking them the same question. He responded that now he had different answers.

This is at the heart of sustainable development and I believe a guiding principle of EcoVision.

Environmental action program EcoVison II (2002-2005)

Improvements	Targets (cumulative)		Results (cumulative)		
Product improvements	Mandatory	Recommended	Not realized	Realized vs mandatory target	Realized vs recommended target
EcoDesign	Level 6 on maturity grid	Level 8 on maturity grid	[1]	-	-
Green Flagship products	One per PD per year	One per BU per year	-	>160	-
Supplier management	Level 6 on maturity grid	Level 8 on maturity grid	[2]	-	-
Process improvements	Mandatory target (reductions)	Recommended target (reductions)	Not realized	Realized vs mandatory target	Realized vs recommended target
Energy	10%	20%	-	-	25%
Waste	20%	30%	-	23%	-
Water	15%	20%	-	-	36%
Emissions to air and water					
Restricted substances	70%	90%	-	-	93%
Hazardous substances	30%	50%	-	-	94%
Relevant substances	15%	30%	-	-	46%
Packaging	Maintain performance	10%	-	2%	-
ISO 14001 certification	All manufacturing sites	All facilities	93%	-	-

[1] This parameter is not reported at Philips Group level [2] Use of this parameter has been discontinued

EcoVision II

Guided by the basic principle that prevention is better than cure, we work to minimize the impacts of our products, processes and services. To meet this challenge, we began establishing a series of four-year action programs more than a decade ago:

- The Environmental Opportunity (1994-1997)
- EcoVision I (1998-2001)
- EcoVision II (2002-2005)
- EcoVision III (2006-2009)

As the chart above illustrates, we achieved all but one of the targets we set for ourselves with our EcoVision II program.

2005 results

Packaging

As a result of EcoVision II, a comparable reduction of 2% packaging reduction was achieved against the base year of 2001. Sizeable reductions in Lighting were realized by intelligent design of packaging volume per product, which offset the relative increases in Consumer Electronics and Domestic Appliances and Personal Care, caused by trends to larger products and marketing requirements for display and anti-theft.

Energy

We surpassed the mandatory EcoVision II target of a 10% reduction in energy consumption, as well as the recommended target of 20%. The comparable decrease in energy consumption at company level was 25% against the base year 2001. Semiconductors and Lighting both achieved a 24% reduction through cost-reduction programs, renewal or optimization of production equipment, and more efficient production.

Waste

We exceeded our EcoVision II target of a 20% reduction in total waste, including recyclable waste, against the base year of 2001, achieving a 23% reduction. Lighting achieved a 23% reduction, or a 56% share of total, comparable with 2001, driven by focusing on cost reduction and efficiency in production processes.

Water

We exceeded our EcoVision II target of 15%, compared to the base year of 2001, achieving a 36% reduction in comparable terms. Semiconductors' cost-reduction and water-recycling programs had a major impact on this achievement.

Restricted substances

On a cumulative basis, we realized a 93% reduction of restricted substances, compared with the base year of 2001, exceeding the EcoVision II target by 23 percentage points. This is mainly due to the replacement of restricted substances with water-based alternatives.

Hazardous substances

The comparable decrease in hazardous substances against the base year is 94%, exceeding the EcoVision II target by 64 percentage points. Lighting's program to eliminate toluene and xylene has made a major contribution to this achievement.

Relevant substances

Lighting's application of oxy fuel technology in the glass furnaces causing less emission of NO_X and SO_2 and Semiconductors' process improvements are responsible for the comparable decrease in relevant substances versus the base year of 2001 of 46%, exceeding our EcoVision II target by 31 percentage points.

Products

Our EcoDesign procedures deal with all phases of product development. To support the EcoDesign process, our EcoVision programs require improvements in the following Green Focal Areas:

Energy consumption | Packaging | Hazardous substances | Weight | Recycling and disposal | Lifetime reliability

Green Flagships

To be considered a Green Flagship, a product must first go through divisional EcoDesign procedures. Next, the product or product family is investigated in at least three of our Green Focal Areas. Based on this analysis, the product or product family must be proven to offer better environmental performance in at least two Green Focal Areas – or in one Green Focal Area plus a 10% improvement in the overall Life Cycle Score, calculated with our EcoScan tool.

During this investigation, a product or product family is compared with its predecessor or closest commercial competitors. When 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.

So while a product may be 'green', only our top EcoDesigned products achieve Green Flagship status.

With 50 Green Flagships launched on the market in 2005 we more than doubled the 2004 total of 21. Illustrating our commitment to enhance energy efficiency, 34 of these Green Flagships offer improved energy consumption. Our total number of Green Flagships on the market is more than 160.

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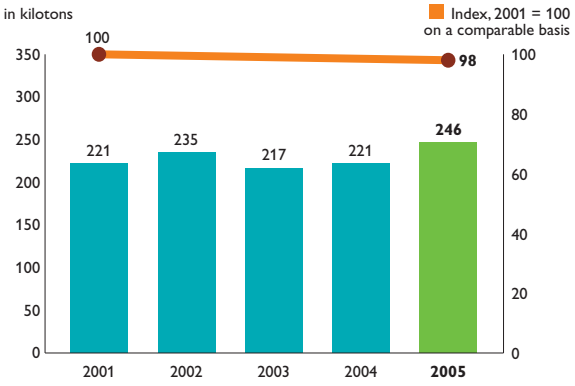
Packaging

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

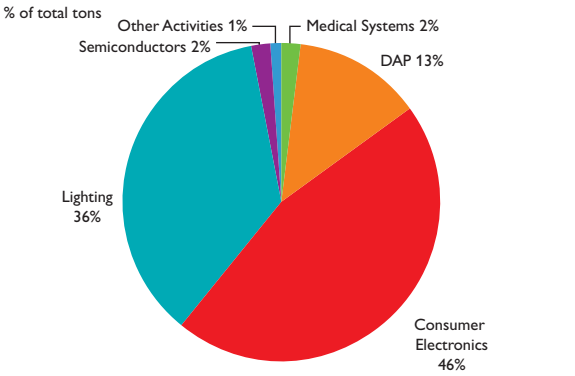
Total packaging material



Philips packaging materials in 2005 amounted to 246 kilotons, an absolute increase of 11% from 2004. In comparable terms with respect to 2004, packaging materials decreased by 2%.

Consumer Electronics, accounting for 46% of the total, showed an absolute increase of 11%, caused by the trend to larger screen sizes. Philips Lighting, accounting for 36% of the packaging total, remained at the same level as 2004.

Total packaging by sector in 2005



Green Flagships

Digital radiography

PCR Eleva systems provide significant improvement in image quality while preserving the images' natural appearance. Simplification and customization of workflow according to individual requirements allows technologist's to spend a maximum amount of time caring for patients. Compared to its predecessor, PCR Eleva reduces energy consumption by 41% in normal use and 43% in standby. Plus, it weighs 17% less and uses 15% less packaging.

Designed for real world use

Our HeartStart FRx Defibrillator is designed to be easy to use, rugged and reliable for first responders. Weighing in at just 1.6 kilograms – 28% lighter than its predecessor – the FRx Defibrillator is the solution for treating Sudden Cardiac Arrest from ventricular fibrillation in environments and conditions too demanding for many other defibrillators.

Medical Systems

Philips Medical Systems is a leader in breakthrough technology and in realizing environmental innovations. By integrating EcoDesign into the product creation process, designers can target the environmental impact of the full product cycle, from design through production and end-of-life. The end result? Environmentally sound design and innovation for the healthcare market.

The latest innovations in MR

We're changing the way the world looks at magnetic resonance, creating higher-quality images and expanding the breadth of applications. The Panorama 1.0T open MR system's open design ensures patient comfort, while our innovative SmartExam feature increases operator efficiency by 30%. This system weighs 58% less than the competition and uses 14% less energy.

Domestic Appliances and Personal Care

Philips Domestic Appliances and Personal Care has long been at the forefront of making packaging out of recycled material. We have taken significant steps in this area and also focus on reducing the weight of our products.

Relax and revitalize

Our Innergize meets the needs of busy consumers looking for solutions to revitalize. Combining tanning, infrared warmth as well as natural scents and sounds, the Innergize creates a relaxing experience and a sense of wellbeing. After use it can be folded up to a compact size and stored away easily thanks to its lightweight design. The Innergize is 45% lighter and uses 3% less energy than its predecessor.

Breathtaking natural pictures

The FlatTV 37PF7320A offers superior picture quality with the latest LCD technology and Pixel Plus. This 37-inch LCD TV uses 39% less energy and 24% less packaging than our closest commercial competitor. Plus, this TV is lead-free and complies with stringent EU legislation.

Smart Choice

Consumers can enjoy the best sound quality in the most straightforward and easy to use phone, our DECT 525. This telephone consumes 54% less energy and uses 14% less packaging than the average of our commercial competitors. It's also 33% lighter and improves recycling and disposal 12%. And we have eliminated cadmium, lead and mercury from this phone.

Pumping up productivity and performance

The compact 190S6 LCD monitor meets the highest international safety and ergonomic standards. Users experience optimized viewing thanks to the monitor SmartBright feature. This 19-inch monitor is 12% lighter than the average weight of the closest commercial competitors. With its energy saving performance averaging 17% less, this LCD monitor offers the lowest total cost of ownership. Ahead of legislation, this LCD monitor is cadmium, mercury and lead free.

Touch your tunes and photos

With this GoGear HDD 1620 you can effortlessly enjoy your world of MP3s and WMA music and pictures. The Micro Jukebox uses 47% less energy and is 12% lighter than the average of closest commercial competitors. And it's already lead-free.

Consumer Electronics

Typical contributions of energy consumption during the useful life of consumer electronics products range from 70-90% of total environmental impact. To reduce the impact of our products, the EcoDesign procedures at Philips Consumer Electronics require Green Flagship products to be 10% more energy efficient than the competition. It's about taking EcoDesign to a higher level, dealing with environmental impacts at the outset during the product creation process and, thereby, driving innovation.

Full details on Green Flagships can be found on page 75.

Unlike any other

Our new S2 and S10 starters are the most reliable, safe and environmentally friendly starters in the world. They contain no hazardous substances and offer a 42% longer lifetime than the average of the closest commercial competitors. Unlike other starters on the market, Philips starters do not contain radioactivity inside their glow switch for ignition.

Small and bright

This TV projection lamp may be smaller than its predecessor, but it offers increased light output. In comparison, this UHP lamp uses 50% less energy and 52% less packaging, and improves lifetime 25%, compared with its predecessor.

Lighting

Philips Lighting continuously explores ways to maximize energy efficiency to lower CO_2 emissions and energy costs. We work to improve product lifetime and reliability to reduce waste and maintenance disruption. Plus, we are setting the pace in mercury reduction, as well as in lead-free and radioactive-free products.

Thinking small so our customers can think big

Mini MasterColor® lamps are ideal for accent and display lighting, in specialty retail, hospitality and architectural outdoor applications. Breakthrough technology means better light quality, longer life and better energy efficiency than standard halogen lamps. The Mini MasterColor 20W lasts twice as long and uses half the energy consumption, compared to standard halogens used in the same application.

More light, longer life

Our MASTER PL line of compact fluorescent lamps offer the lowest mercury content in the industry, are energy efficient and reliable. The MASTER PL-C 2pin lamps improve lifetime 33% and contain 56% less hazardous substances, compared with the average of our closest commercial competitors. And their glow switches are free of radioactivity.

Semiconductors
Product design at Philips Semiconductors is driven by miniaturization and energy efficiency, benefiting the environmental performance of our products and their applications. Our products are lead-free well before the new legislation comes into effect on July 1, 2006. Our new chemical content database provides easy access to product information, making the move to lead-free an easy path for customers to follow.

Easy to use

Our ANT2216 is an internal active antenna for portable TV applications like PDAs. Eliminating the external antenna, housing and cable makes it easy for the end-user to carry and operate the device. This antenna uses 40% less energy, offers 85% lower product weight and improves recyclability 47%, compared with its competitor.

Crisp, clear sound

Combining high audio quality and very high power, our Discrete Class D High Power Audio Amplifier 5TG 96517 is a leader in its segment. This amplifier module uses 22% less energy, 37% less packaging and weighs 67% less than its predecessor.

Integration and innovation

The BGY 504 semiconductor module integrates a power amplifier, antenna switch and power loop for mobile phones into one new product. This high degree of integration makes design-in for customers easier. The product needs 14 fewer external components and the printed wiring board size is 36% smaller than its predecessor. It uses 25% less energy, is 18% lighter and uses 33% less packaging.

Less is more

The TEF6901 AM/FM world receiver for car radio applications goes beyond standard features, providing continuous IF band-width control to improve adjacent channel suppression – a Philips invention that has become the world standard for high-end car radios. Compared with its predecessor, this IC's chip size is 36% smaller and it requires 25% less external electronic components. Plus, it uses 22% less energy and 19% less packaging.

Optical Storage
Philips Optical Storage meets the needs of its customers for environmentally sound products by integrating EcoDesign procedures into the design process. Information on the content of environmentally relevant substances is available for all products and all products will be lead-free well in advance of legislative requirements.

A key component

The OPU66.43 Optical Pickup Unit is a key component in a DVD Writer drive for DVD R/RW. This innovative product offers significant reductions in hazardous materials – 75% less cadmium and 99.7% less lead – than its predecessor. And it uses 29% less packaging material.

Full details on Green Flagships can be found on page 75.

Production

We have long strived to make effective use of resources and have set targets to optimize our processes. The aim is to reduce environmental impacts, achieving cost savings and improved 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. The company also recommends that all non-industrial facilities obtain certification.

Percentage of reporting organizations ISO 14001 certified

The percentage of certified units at year-end 2005 was 93% compared to 94% in 2004. This includes six newly certified reporting organizations and four whose certificates expired.

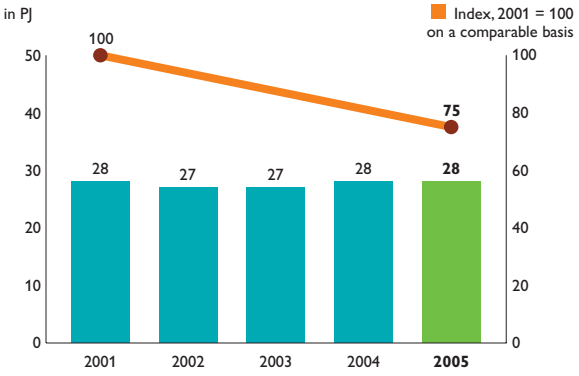
Energy

EcoVision 2002-2005 called for a 10% reduction in energy use.

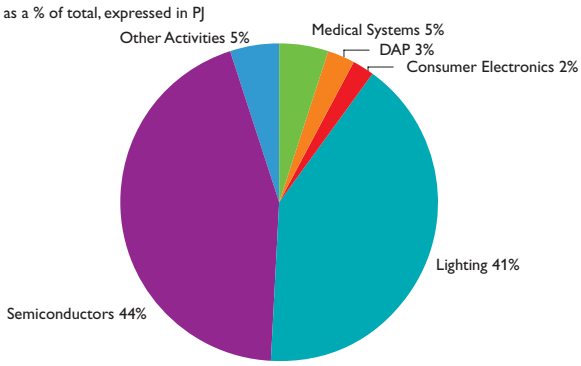
Absolute energy consumption amounted to 28.4 PJ, level with 2004. However, after correction for a production increase of 2%, we realized a comparable decrease of 2% versus 2004. Lighting and Semiconductors are responsible for 85% of total energy used in our production processes.

In 2005, 76% of all energy consumption was purchased as electricity with 20% gas, remaining at the 2004 level.

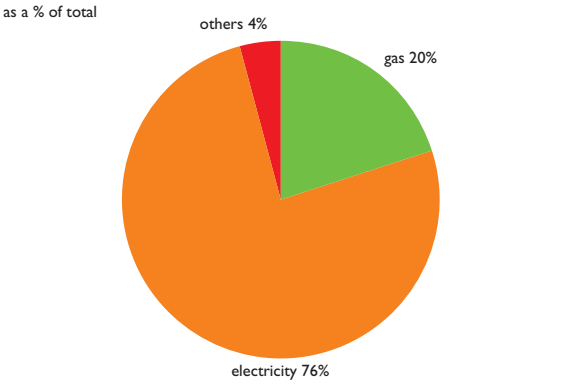
Total energy consumption



Total energy consumption by sector in 2005



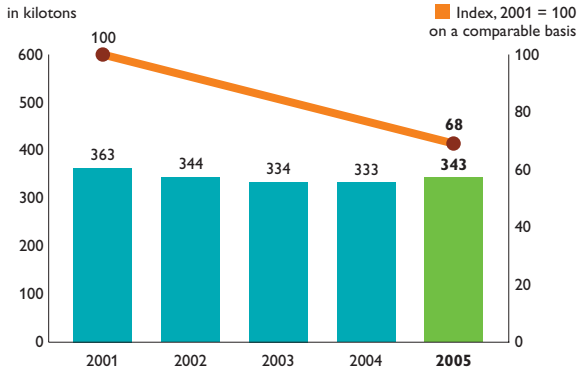
Total energy consumption by source 2005



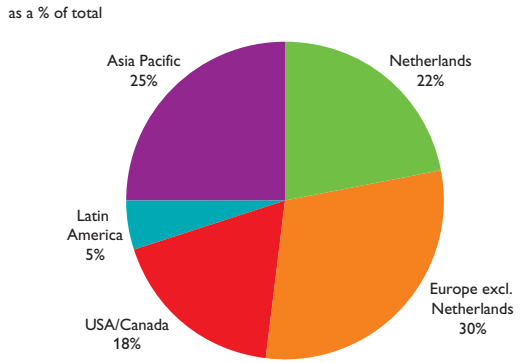
CO_2 emissions

Direct CO_2 emissions from production in 2005 amounted to 343 kilotons, compared to a comparable 333 kilotons in 2004. Lighting was responsible for 77%, mostly attributable to emissions from glass furnaces.

Total direct CO_2 emissions



Direct CO_2 emissions by geographic area in 2005



PFCs

Philips emitted 575 metric kilotons equivalent CO_2 in the form of PFCs in 2005, compared with a comparable 710 metric kilotons in 2004, attributable to Semiconductors. The Global Warming Potential of a greenhouse gas is the ratio of global warming (or radiative forcing) – both direct and indirect – from one unit mass of a greenhouse gas to that of one unit mass of carbon dioxide over a period of time.

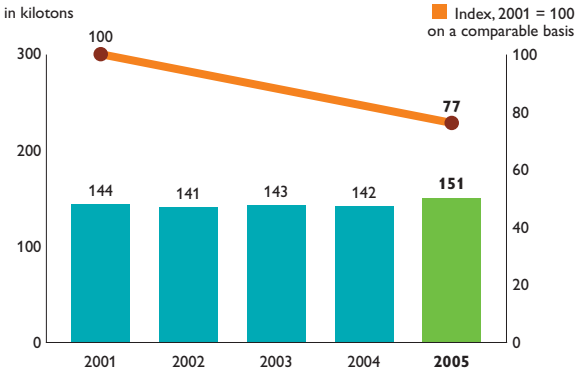
Our Semiconductors division participates in the industry's Semiconductors Voluntary Agreement, which calls for a 10% reduction in PFCs in 2010, based on 1995 levels.

Waste

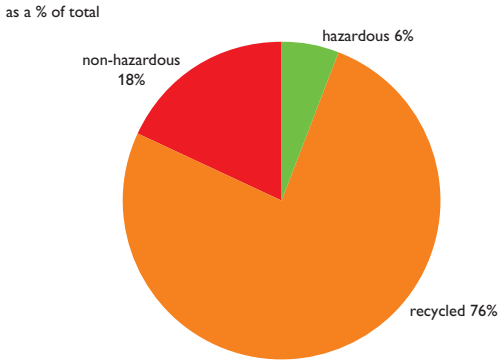
Philips disposed of 151 kilotons of total waste in 2005 – a nearly 7% increase in absolute terms compared with 2004. This increase is due to the reporting of one-time waste, such as major demolition, rebuilding, reallocation and natural disaster (flood).

Semiconductors achieved a 13% relative reduction in 2005, compared with 2004. Consumer Electronics saw a 29% increase in trend, compared with 2004, which is largely attributable to packaging of parts shipped from Asia to central assembly plants.

Total waste



Composition of total waste in 2005

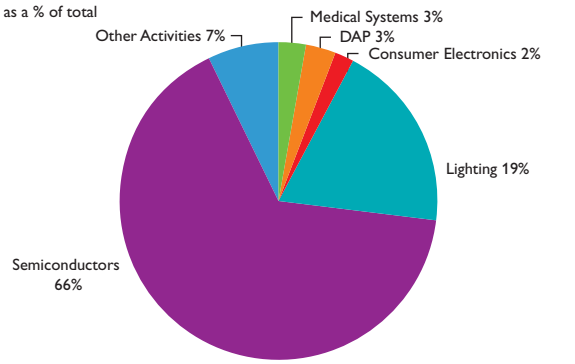


Total waste is made up of actual waste that is delivered for either landfill or incineration, and recyclable waste. Actual waste delivered for landfill or incineration comprised 18% non-hazardous and 6% hazardous waste, with the remaining 76% (or 114 kilotons) delivered to recycling companies.

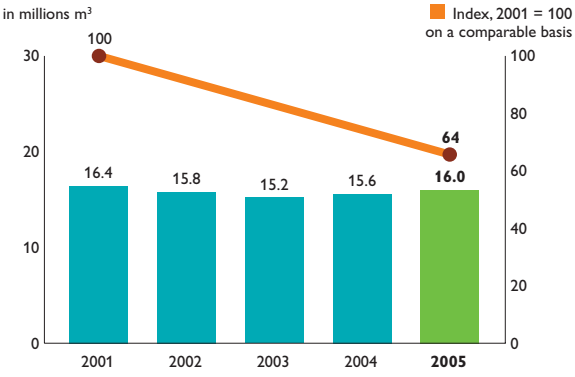
Water

The amount of water used in 2005 (16 million m^3) increased by 3% in actual terms, compared to 2004, with Semiconductors contributing to 66% of the total. Semiconductors and Lighting are the major users of water in production processes, and have conducted water- and cost-savings programs to achieve reductions.

Total water intake by sector in 2005



Total water intake



Emissions to air and water

Restricted substances

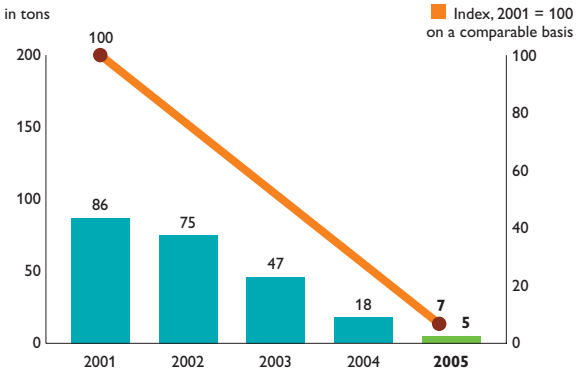
In 2005, 5 tons of restricted substances were emitted – a 71% decrease in absolute terms compared with 2004. Only Medical Systems and Lighting, with 58% and 42% of the total Philips share respectively, contribute to these emissions.

Increased production in Medical Systems accounted for an increase in the emission of these substances, as did equipment maintenance issues and a relocation of transducers combined with poor production yields.

Two new VTL (mercury flush) production lines were largely responsible for Lighting's higher emissions.

By replacing restricted substances with relevant substances, both the Semiconductors and Other Activities product divisions eliminated the missions of restricted substances altogether.

Total restricted substances

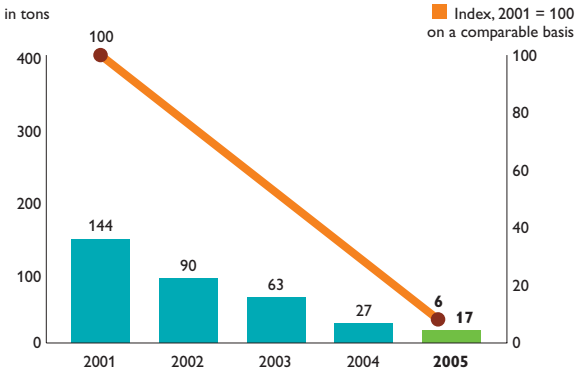


Hazardous Substances

Hazardous substances shows a 38% downward trend in absolute terms compared with 2004. Lighting is the main contributor to these emissions, with 70% of Philips total share. Lighting achieved a reduction by replacing 2-ethoxy ethanol by water-based coatings and introducing lead-free soldering.

The PFCs emitted exclusively by Semiconductors are no longer being reported as emission of hazardous substances, but as Global Warming Potential.

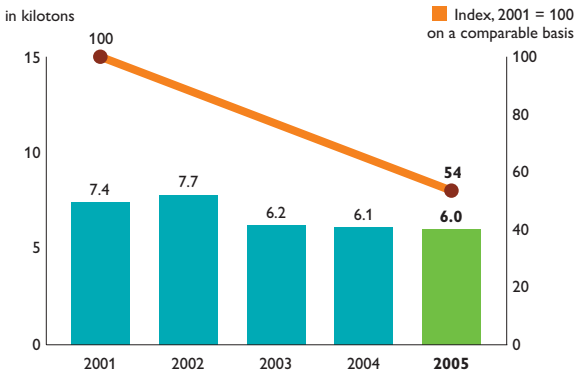
Total hazardous substances



Relevant Substances

Relevant substances remained largely unchanged in 2005 compared to 2004. Lighting and Semiconductors contribute almost equally to 97% of the total emission of relevant substances.

Total relevant substances



Legal compliance

Compliance issues are resolved through local management with legal counsel.

For information about provisions for environmental remediation please refer to page 164 of the Annual Report.

In 2005 Philips incorporated the registration of fines related to non-compliance issues in its reporting systems. An amount of EUR 3,000 was reported.

Incidents

In 2005, 29 incidents were reported in eight categories. They were related to water (three), waste (one), soil (one), fire (one), packaging (one), and emissions of restricted substances (one), hazardous substances (one) and relevant substances (20).

EcoVision III (2006-2009) environmental action program

After having successfully completed our EcoVision II environmental action program, we are beginning a new four-year program to improve our overall environmental performance.

In the course of 2005, a cross-divisional task force worked on the preparation of this new program. As a first step, the main environmental trends and issues where identified and an extensive benchmark study was conducted. We defined our priorities using the following criteria: Philips' possibilities to influence, societal relevance, reputational and non-compliance risk, and our position versus our benchmarks.

Product improvements

We continue to work to improve the environmental performance of our products, using our Green Focal Areas to drive our EcoDesign processes. Improvements will be measured yearly via one of our Key Performance Indicators (see page 16).

Process improvements

The aggregated Philips' Group targets for process improvements are included in the table below. For efficiency and simplicity reasons, the scope has been limited to those divisions, contributing at least 90% of our environmental impact per parameter. Also for simplicity reasons, reduction targets have been set in absolute terms, against the base year 2005.

Although the major environmental impact of our facilities lies in production, we identified our non-industrial facilities, such as offices, logistic centers and research and development. We have decided not to report on non-industrial activities, because their contribution is not material.

EcoVision III (2006-2009)

Improvements	Targets
Product improvements	
Yearly target set on number of Green Flagships: 2006	35
Process improvements*	
Global Warming Potential (CO_2 equivalents)	
Energy reduction (direct CO_2)	5%
PFC reduction	31%
Other greenhouse gas reductions	4%
Water	7%
Total waste	7%
Restricted substances: benzene emissions	100%
Restricted substances: mercury emissions	83%
Restricted substances: CFCs/HCFCs	94%
Other restricted substances (excluding CFCs from cooling systems)	100%
Hazardous substances: PFC emissions	31%
Hazardous substances: lead	100%
Hazardous substances: toluene	100%
Hazardous substances: xylene	100%
Other hazardous substances	100%

* Total reduction targets in absolute terms, against the base year 2005

Our economic

Highlights

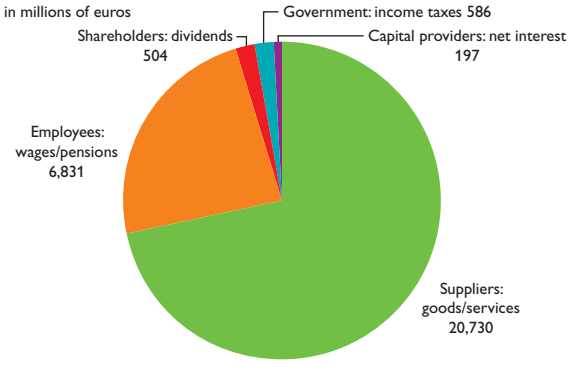
- Market capitalization increased EUR 7 billion
- EBIT margin up to 5.9%
- Debt-free balance sheet

2005 was a good year for our company. We made further progress on our journey to transform Philips into a truly market-driven healthcare, lifestyle and technology company. One that is capable of delivering sustained profitable growth. We took a number of decisive steps that have created tangible value, and our market capitalization increased by some EUR 7 billion.

Economic stakeholders

In addition to our shareholders, many other stakeholders have a direct interest in our economic performance, as illustrated below in terms of cash flow.

Distribution of economic benefits 2005

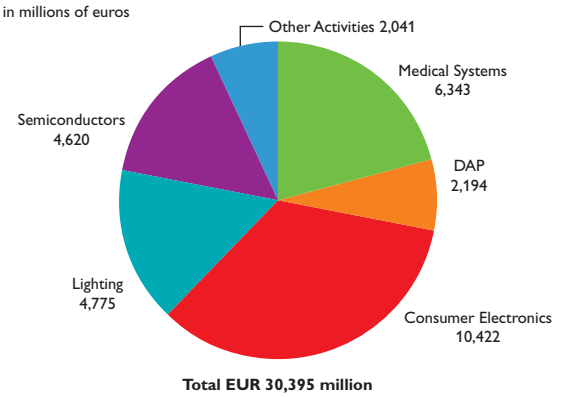


Customers

Sales of the Philips Group

Sales in 2005 amounted to EUR 30,395 million compared with EUR 29,346 million in 2004, an increase of 4% nominally as well as at a comparable basis. The appreciation of the US dollar and other currencies had a positive net impact of 1% on sales, which was offset by consolidation changes. Comparable sales growth in 2005 was particularly strong at Medical Systems and DAP. The 7% growth at Medical Systems was driven by all businesses except MedQuist and Medical IT. The 6% growth at DAP was mainly attributable to Food & Beverage and Shaving & Beauty.

Sales per sector 2005



performance

CE grew nearly 5%, driven by Connected Displays (strong growth in flat display TVs) and Home Entertainment Networks. In the Lighting division, Lighting Electronics and Luminaires were the main drivers of the 4% growth. Semiconducters' sales level approximated 2004, despite the less buoyant cycle for the greater part of 2005. Other Activities sales declined almost 18% in nominal terms due to the divestment of certain non-strategic activities within the Corporate Investments portfolio.

Geographic sales distribution

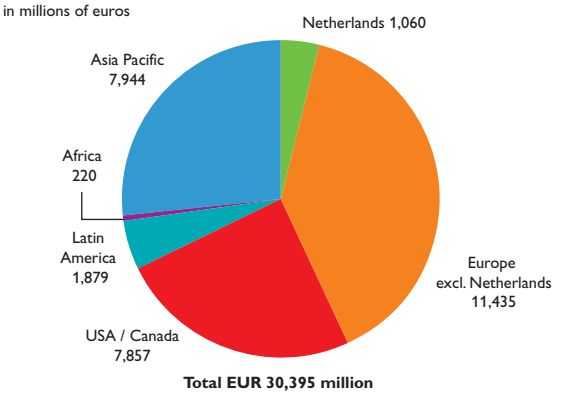
Sales in Europe and Africa declined by 2% in 2005 with divestments having a downward effect of 1%. The decline was mainly visible in the Semiconductors division (a nominal decline of 7% due to the shift in sales to manufacturers in Asia) and in Other Activities, whereas Medical Systems, DAP and Lighting showed a nominal sales increase of 3%, 6% and 6% respectively.

Sales in North America showed a strong increase of 7%, and were particularly strong in CE, which benefited from the positive impact of the business renewal program and strong demand for flat TVs and DVD recorders with hard-disk functionality.

Sales in Asia Pacific increased by 5%. Growth was visible in all divisions except CE, which benefited from past-use license agreements in 2004. Double-digit growth was visible at Medical Systems, DAP and Semiconductors on a nominal basis.

Latin America posted exceptional sales growth of 31% nominal, attributable in part to the positive effects of currency movements. Excluding these currency effects, the region nevertheless showed strong comparable growth of 19%.

Sales by geographic area 2005



Employees

Wages

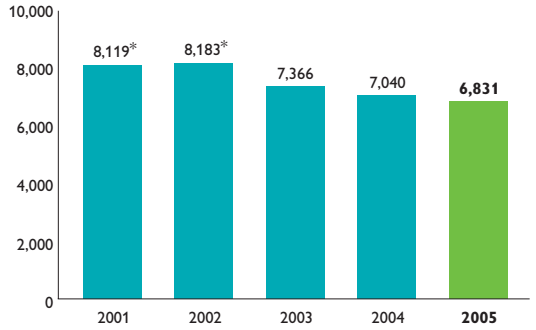
The composition of our workforce and the changes in 2005 has been addressed in the employee section of this report.

The economic benefits for our employees are the direct and indirect wages. The total amount of wages in 2005 amounted to EUR 6,831 million and was composed of the following elements:

in millions of euros	
Direct salaries and wages	5,833
Pension costs	258
- Required by law	755
- Voluntary	(15)
Total	6,831

Total wage bill development

in millions of euros



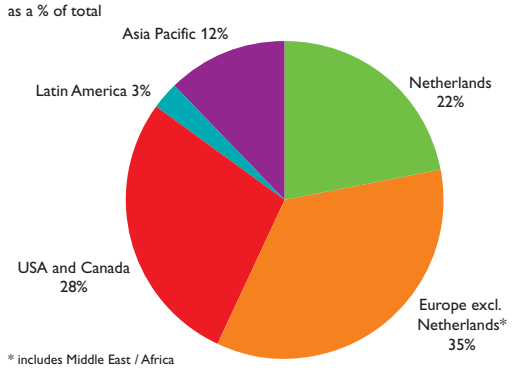
* 2001-2002 have not been restated to present the MDS activities as a discontinued operation

The total wage bill decreased 3% in 2005, compared with the year before. The main reasons for this decrease are:

- The reduction of pension costs, from EUR 281 million to EUR 258 million in 2005.
- Lower social security and similar charges decreased strongly from EUR 970 million in 2004 to EUR 740 million in 2005. Post-retirement benefit costs included EUR 116 million from a total provision release of EUR 187 million. The latter was triggered by a change in Dutch law relating to the treatment of medical insurance costs.
- The decrease in the number of our employees (2.7% on average basis).

Wage bill per geographic area in 2005

as a % of total



* includes Middle East / Africa

Excluding pension costs and social security charges, the wage bill increased 1%, or 3.5% per employee.

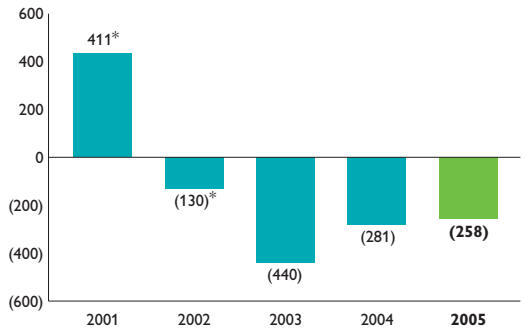
Employee pension plans have been established in many countries in accordance with the legal requirements, customs and the local situation in the countries involved. The majority of employees in Europe and North America are covered by defined-benefit pension plans. The benefits provided by these plans are based on employees' years of service and compensation levels. The measurement date for all defined benefit pension plans is December 31.

Contributions are made by Philips, as necessary, to provide assets sufficient to meet the benefits payable to defined-benefit pension plan participants. These contributions are determined based upon various factors, including funded status, legal and tax considerations as well as local customs.

After strong increases in total pension costs between 2002-2003, a reverse trend was posted in 2004, which continued through 2005.

Total pension (costs)/benefits

in millions of euros



* 2001-2002 have not been restated to present the MDS activities as a discontinued operation

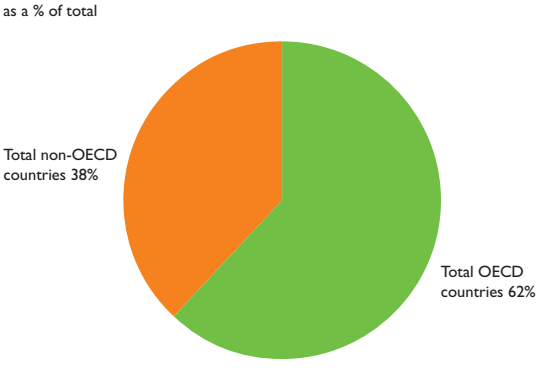
Suppliers

Total products and services purchased in 2005 amounted to EUR 20.7 billion, representing 68% of total sales. For further details see pages 66-70.

The economic impact on non-OECD countries amounts to EUR 7.8 billion, 38% of our overall spend.

Total purchased products and services in 2005

as a % of total

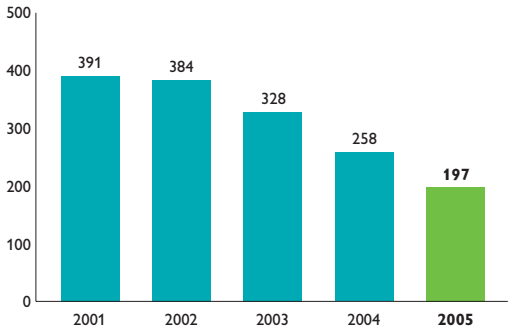


Providers of capital

The total amount of net interest expenses decreased further in 2005 to EUR 197 million, as a result of a strong decrease in net debt and increased interest income.

Total interest expenses (net)

in millions of euros



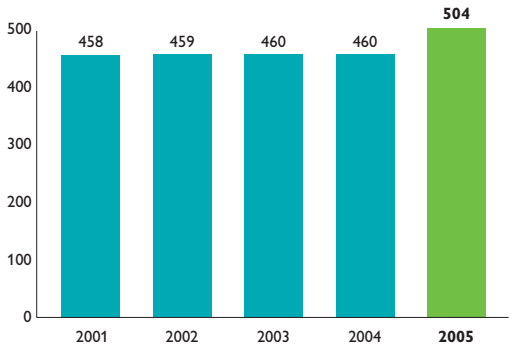
Shareholders

Dividends

In line with our dividend policy, an amount of EUR 504 million or EUR 0.40 per common share was paid as dividend to shareholders in 2005. A proposal will be submitted to the General Meeting of Shareholders to declare a dividend of EUR 0.44 per common share.

Total dividends

in millions of euros



Government

Income taxes

Income taxes amounted to EUR 586 million, compared to EUR 358 million in 2004. Income taxes in 2005 included an amount of EUR 240 million related to the transfer of shares of TSMC to the company from its fully owned subsidiary Philips Electronics Industries Taiwan Ltd. This was partly offset by a EUR 119 million tax gain relating to final agreements on prior years taxes in various jurisdictions. The tax burden in 2005 corresponded to an effective tax rate of 31.1% on the pre-tax income, compared to an effective tax rate in 2004 of 19.9%.

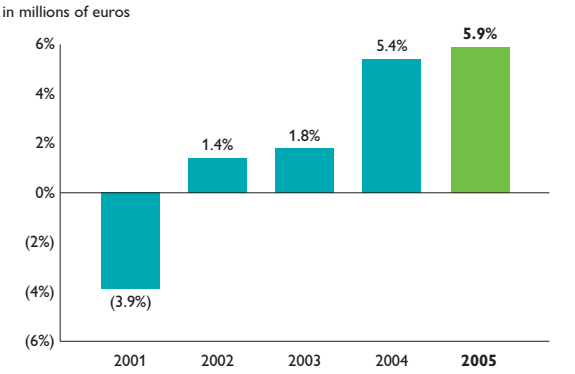
Financial performance in 2005

Net income in 2005 amounted to EUR 2,868 million compared to EUR 2,836 million in 2004. The comparability of the income is impacted by several significant transactions in both years. Included in 2005 was EUR 1,778 million from the sale of financial holdings (TSMC, LG.Philips LCD, NAVTEQ, Atos Origin, Great Nordic).

Earnings before interest and tax (EBIT, previously IFO) amounted to EUR 1,779 million in 2005, compared to EUR 1,586 million in 2004.

Earnings before interest and tax as a % of sales

in millions of euros

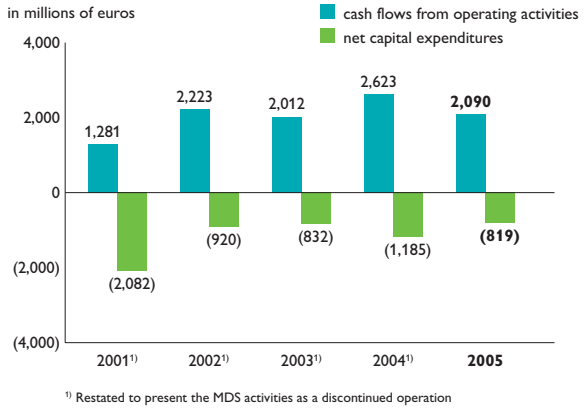


The following overview aggregates sales and EBIT.

in millions of euros	2005		
	sales	EBIT	as a % of sales
Medical Systems	6,343	679	10.7
DAP	2,194	358	16.3
Consumer Electronics	10,422	506	4.9
Lighting	4,775	556	11.6
Semiconductors	4,620	307	6.6
Other Activities	2,041	(156)	(7.6)
Unallocated	–	(471)	–
	30,395	1,779	5.9

In 2005, net cash provided by operating activities amounted to EUR 2,090 million, compared to EUR 2,623 million in 2004, mainly reflecting higher working capital needs, particularly in Medical Systems and Lighting. Inventories as a percentage of sales at the end of 2005 increased to 11.4%.

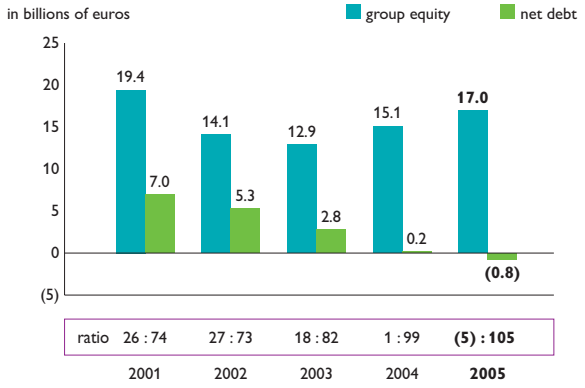
Cash flows from operating activities versus net capital expenditures



[1)] Restated to present the MDS activities as a discontinued operation

Stockholders' equity increased by EUR 1,806 million to EUR 16,666 million at December 31, 2005. The net cash position (cash and cash equivalents, net of debt) was EUR 806 million at the end of 2005, compared to a net debt position at the end of 2004 of EUR 164 million. On a net basis, our Philips company is now debt-free, which will allow us to pursue our growth plans.

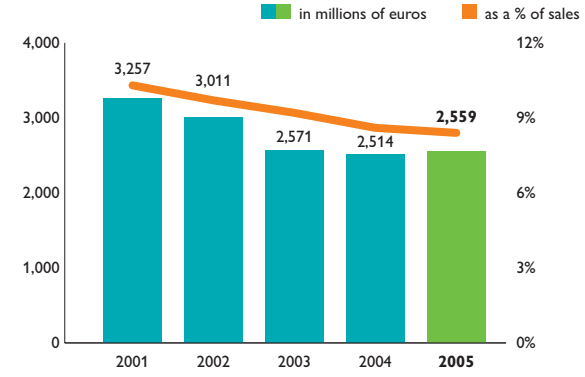
Net debt to group equity



Technology

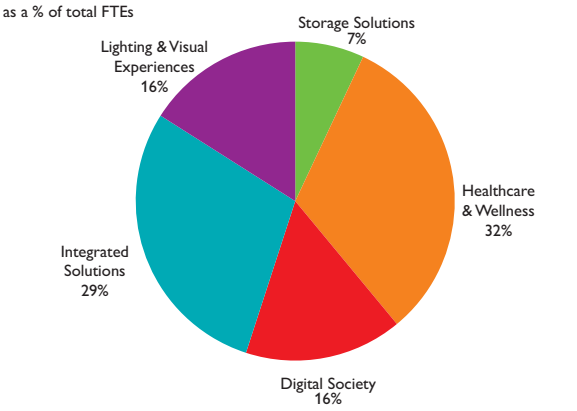
Our research and development expenditures totaled EUR 2,559 million, or 8.4% of sales, compared to 8.6% in 2004.

Total Philips research and development expenditures



The stabilization of the research and development spend reflects actions taken to balance the overall Philips portfolio, such as the outsourcing of the monitor and low-end flat TV activities to TPV, as well as the pro-active re-balancing of research and development expenditures in line with the company's healthcare, lifestyle and technology focus areas.

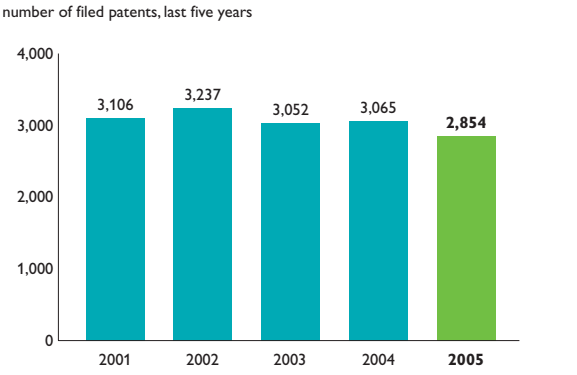
Research programs in Corporate Technologies



In 2005, Medical Systems saw an increased research and development spend in the areas of molecular medicine and new sensor technologies, Lighting in LCD backlighting, DAP in Consumer Health & Wellness and Semiconductors in Home and Mobile & Personal activities. Research and development expenditure has also been aligned to the healthcare, lifestyle and technology focus areas, including the establishment in late 2005 of two new research incubators for healthcare and lifestyle (breeding grounds for new, innovative product concepts). As a result, the relative amount of research invested in the more traditional areas of integrated circuits and imaging technologies has been reduced.

Despite slightly lower research and development expenditures we maintained our high level of first filings of patents. In 2005 we filed 2,854 new patents. By year-end 2005 the total number was 23,062 patent families.

New patents continue at high level



Sustainable value creation

Gerard Ruizendaal
Executive Vice President
Strategy & Control
Member of the Sustainability Board

As an economist I have always been surprised by the contradiction that has been created between sustainability and business interests. In fact the founding father of free market economics and economic science, Adam Smith, started his work on economics because of his worry about the contradiction between the common interest and the private interest. It was the 18th century, and people started to discuss democracy, human rights, equality, rule of law and free markets as an alternative to serfdom and absolute government. But how relevant is the thinking of an 18th century philosopher in today's global information society? How relevant is it for Philips' policies?

Adam Smith tried to answer the question: If people are free to pursue their own interests, how can we avoid a downward cycle where individual optimization leads to society as a whole being destroyed? In his 1776 book, *Wealth of Nations*, he showed how a market economy promotes the advancement of society as a whole, but in his less-known 1756 book, *Theory of Moral Sentiments*, he explains how it is in the interest of free citizens to look to the common interest in order to advance their own interest. Both the scientific and ethical foundation of market economics can be found in 18th century worries about sustainability.

Two sides of the same coin

Things have not changed – in the 18th century when Adam Smith wrote his books, in the 19th and 20th centuries when Philips became a major multinational company and now in the 21st century. The legitimization of a company lies in its contribution to society, by innovation, by creating business, but always with the understanding that pursuit for value creation is in the end value creation for society at large. From its founders, the brothers Philips, onwards, Philips has always understood that pursuing business interest and feeling responsible for sustainability is not a contradiction, but in essence two sides of one coin. It is this understanding that good business and sustainability belong to each other that makes working for Philips very rewarding to me.

You find this back in our mission statement "bringing meaningful innovations to improve the quality of people's lives". A contradiction with value creation? No, not at all. People value innovations that improve their life. If they value our innovations, they will show that by paying for them and thereby creating value for the company.

Often a contradiction is seen between short-term interests and long-term interests – capital markets force companies to focus on the next quarter and not on long term business development and innovation. But let us have a look at the empirical evidence. Do countries where the shareholders are more influential have lower long-term growth rates and lower levels of innovation? On the contrary, normally we see that countries without markets perform worse.

Valuing long-term growth potential

From a company perspective we see that investors value most the companies that have a solid long-term growth potential. It is not good enough to have a good quarter. Investors want to see a roadmap for longer-term sustainable profitable growth. It is like in football, to win the competition is the long-term goal, but winning every match is the way to get there.

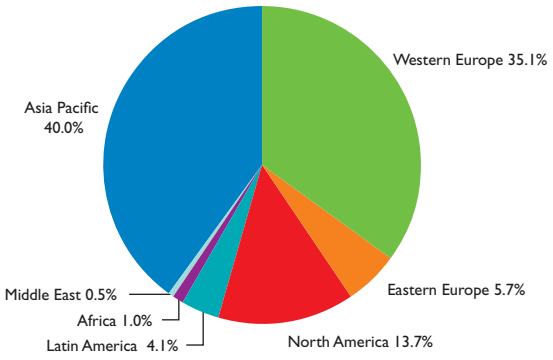
In September 2005, the Group Management Committee had a discussion on how to speed up profitable growth. Next to innovation of product and service offerings, a lot of attention was given to emerging markets, including bottom of the pyramid opportunities. There are many possibilities for additional profitable growth in these markets. Good examples are water and air purification where we can improve the quality of people's lives using our technologies to keep people healthy. We will be able to create sustainable businesses generating a return for our financial stakeholders while at the same time contributing to sustainable development. Another example is energy efficient lighting that could enable developing countries to grow with less use of oil and less environmental problems.

In the growth initiatives of Philips, emerging markets and sustainability will be key focus elements because it both makes great business sense and because it perfectly fits with our mission: to improve the quality of people's lives.

Our suppliers

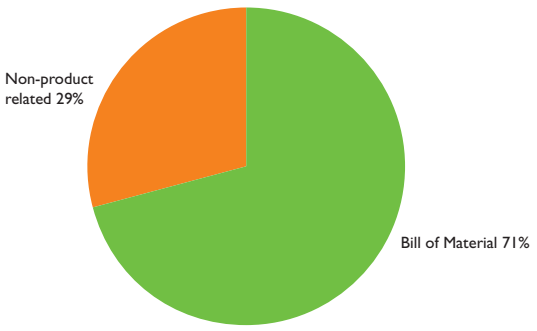
Total purchased products and services in 2005, by geographical area

as a % of total value



Total purchased products and services in 2005, by type

as a % of total value



Highlights

- Number of suppliers reduced by 43%
- 100% return on supplier sustainability self-assessments
- 207 supplier sustainability audits

Philips supply management

A sustainable and capable supply base is indispensable to cope with the accelerating pace of innovation and greatly reduced product lead-times that characterize today's electronics industry. Sourcing is therefore a key part of our supply management strategy, and a high percentage of components and products is purchased rather than manufactured in-house.

Overall the Bill of Materials spend of EUR 15.6 billion is sourced from 6,800 suppliers. Philips also has 18,600 non-product related suppliers that provide a wide range of indirect products and services. During 2005 we further reduced our total number of suppliers from 45,000 to 25,500, with a total spend of EUR 20.7 billion.

With our strategic focus on growth markets, we are consolidating our sourcing in mature markets, while growing our business in emerging regions, especially Asia Pacific. Our focus on 'local for local' solutions also means we are developing our supply base in Eastern Europe and countries such as India, China, Brazil and Mexico.

Transparent e-sourcing

We are increasingly adopting e-sourcing, through which Philips can open a web-based bidding process to suppliers. This process, which is enabled by an online tool, is based on detailed preparation and clear information on our exact requirements, such as technical and logistical specifications. It provides a transparent platform enabling prospective suppliers to bid for sourcing projects in a fair and transparent way, as every step taken is automatically recorded and traceable.

Sustainability in supply management

The Philips Supplier Declaration on Sustainability outlines the minimum expectations of behavior in the critical areas of environment and working conditions. We initially distributed the Declaration to about 2,800 key suppliers. The Declaration is now integrated into the templates in our One Philips General Purchasing Agreement (GPA), which was introduced in 2005.

Our Banned Substances List was also integrated into the GPA templates. Further, we have been actively working with suppliers to ensure that the tens of thousands of components and materials we source comply with the European Union's Directive on the restriction of the use of certain hazardous substances in electrical and electronic equipment, commonly known as RoHS. (See page 49.)

We also provided our supplier self-assessment tool to a group of more than 1,000 suppliers and they all performed the self-assessment and returned it to us. This tool gives them an insight into their social and environmental performance, and we use it to support our audit activities.
www.philips.com/sustainability/report

Training

We continued our sustainability workshop for suppliers during 2005, and have now trained 350 suppliers around the world. We aim to support our suppliers, where needed, in achieving sustainable operations. The workshops give them the opportunity to raise concerns, share best practices and gain an in-depth understanding of our sustainability requirements.

Internally, we have taken steps to raise awareness within the supply discipline. Sustainability has been made part of the Supply Management Core Curriculum, providing our employees with in-depth knowledge of social and environmental issues related to suppliers. Further, we have trained more than 500 Philips managers, qualifying them to conduct supplier audits.

Qualifying managers to conduct supplier audits

Our Mohali factory in Chandigarh, India, was among the Philips facilities that hosted training sessions to qualify our managers to conduct supplier audits, using our modular tool. Participants from various functional areas, including Purchasing, Human Resources, Quality and Internal Audit from Philips India attended the two-day training. Participants focused on how to prepare for and execute an audit.

The training was put to practical use with five actual audits of the Mohali facility's suppliers. Our auditors focused on how factory management deploys and approaches business functions like leadership, quality and sustainability. In order to detect non-compliances with our sustainability requirements, the participants considered worker interviews and detailed facility tours to be vital elements of the audit.

Supplier audits

Considering our extensive supply base, we use several indicators to identify the suppliers to be audited in those cases where we cannot get sufficient assurance of the sustainable behavior of the supplier by other means. These indicators include the country location of the production facility, turnover amount, business risk, the supplier's classification and self-assessment results.

A typical audit is conducted by a multidisciplinary team and includes worker interviews at the production facility, payroll reviews, confirmation of health and safety measures, compliance with relevant national laws and checks for banned substances.

Each audit finishes with a feedback meeting with the supplier, during which the audit results and any non-compliances are discussed. According to the severity of the non-compliance, an appropriate timeline and improvement plan is agreed upon with the supplier. We also register non-compliances in our General Business Principles database.

Our overall approach to ensure suppliers meet our standards is one of finding solutions through open and honest discussions. We expect our suppliers to implement corrective actions if an audit shows that they are not meeting our sustainability requirements and we monitor their progress. If a supplier appears to be unwilling to commit to our sustainability principles or does not follow up on the agreed corrective actions, then our relationship with them can be terminated as a last resort.

During 2005 we conducted 207 audits for existing and new suppliers, mainly in Asia. As a result of our audits, we have identified non-compliances at the facilities of our suppliers and they have been asked to address these issues.

Supply Management/Purchasing Code of Ethics

At the beginning of October 2005, Philips Supply Management issued an updated version of the Supply Management/Purchasing Code of Ethics, which applies to all employees involved in the purchasing process within Philips. It is an integral part of the Philips General Business Principles.
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Appendix

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 the *Philips Sustainability Report 2005* to provide the readers of this 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. The report, including the identification of material issues is our responsibility. Based on the defined scope KPMG decided to perform the activities described in their assurance report.

We realize that building sustainability into our business processes is an ongoing process and that the quality of data collection and analysis and internal controls at product division and corporate level need our continuous attention. As we are in the process of improving this 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, and total direct CO_2 emissions for the years 2001 to 2005 and total global warming potential for 2005.

We have also asked KPMG to perform the activities as listed under 'Environmental data' in the section 'Work undertaken and conclusions' of their Assurance Report on our waste, packaging, restricted, hazardous and relevant substances, and health and safety data to provide us with recommendations for the improvement of the quality of the data and data management systems.

We are in the process of reassessing the scope of the assurance assignment for coming year(s) in order to further optimize the added value of the assurance process for our stakeholders and its contribution to internal improvements. We anticipate that we will have the reliability of information for a selection of material subjects reviewed by an independent assurance provider in the future.

Assurance report

To the readers of the *Philips Sustainability Report 2005.*

Introduction

We have been engaged by Royal Philips Electronics (Philips) to review the *Philips Sustainability Report 2005* (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 2005 financial statements of Royal Philips Electronics, based upon US GAAP.

Limited assurance on whether:

- The data on total energy consumption, total water intake and total direct CO_2 emissions for the years 2001 to 2005 are reliable.
- The data on global warming potential are reliable for 2005.
- 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 page 74 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 74.

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 2005.

Work undertaken and conclusions

Environmental data

For the reliability of the data on total energy consumption, total water intake, and direct CO_2 emissions for the years 2001 to 2005, and global warming potential for the year 2005, we conducted:

- Visits to 17 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.
  - The systems used to generate, aggregate and report these data.

Based on the above, the data on total energy consumption, total water intake and total direct CO_2 emissions for the years 2001 to 2005 and the data on global warming potential for the year 2005 do not appear to be unreliable.

Financial data

We have reconciled the data on financial performance in the sections of the *Philips Sustainability Report 2005* listed below, with the audited 2005 financial statements of Royal Philips Electronics, based upon US GAAP.

- The section 'Key figures' on page 11, excluding the information on 'new patens filed in 2005' and 'patent portfolio (families)'.
- The section 'Participations' on page 12.
- The section 'Our economic performance', excluding the graphs 'Wage bill per geographic area in 2005' and 'Total purchased products and services in 2005' on page 64 and the information on patent filings on page 66.

Based on the above, the data on financial performance, as specified above are properly derived from the 2005 financial statements of Royal Philips Electronics, based upon US GAAP, for which the independent auditors issued an unqualified audit opinion dated February 13, 2006.

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 engagement, diversity and inclusion, health & safety, Philips' role in the community, and suppliers.

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 has made further progress in enhancing the quality of internal control procedures around data collection and reporting at local, divisional and corporate level for environmental, health and safety data. We recommend Philips to attune its reporting systems and internal control procedures to the content of the new environmental programme, EcoVision III. Furthermore we recommend that Philips continues its efforts to improve the quality of its health and safety data.

Philips considers sourcing to be a key part of its business strategy. In this sustainability report Philips explains how it incorporates sustainability in its supply chain. We recommend Philips to report on the sustainability performance of its suppliers in the future.

Amstelveen, February 22, 2006

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 chapters titled Our environmental performance and Our employees.

Environmental performance

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 is available on our external website.

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 2005*, with the exception of MDS, which is considered as a discontinued organization. Data on environmental performance, are still covering the MDS activity for the full year 2005. Environmental data are reported by each manufacturing activity owned, rented or leased and managed by Royal Philips Electronics, with 50 or more people 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 acquisition.
- Data from companies disposed of are excluded in the year of disposal.

Accounting for changes in previously reported data

Data reported in previous years can change as a result of changes in Philips portfolio of businesses or as a result of changes in absolute figures due to improved reporting methods.

Production fluctuations are taken into account by the use of a production index, which is used to calculate relative reductions or increases compared to a reference year – usually the first year of the action program.

For detailed information, see the Reporting Manual on our website.

Organizational changes in 2005

- MDS activities have been moved from Semiconductors to Other Activities.
- Suzhou (China) operations were transferred to TPV.

www.philips.com/sustainability/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.
- Emission of PFC gases is calculated in the EcoVision software using a tool based on Tier 2C Method 2004. To comply with worldwide Semiconductor industry standards, only the Global Warming Potential expressed as CO_2 equivalent should be reported. We have therefore adapted our reporting method to meet with this requirement and no longer report kilograms of PFC as hazardous substances, but as tons of CO_2 equivalent. The data for the year 2004 has, therefore, been restated. PFC data in the years 2001 to 2003 have not been modified because of non-availability of detailed information.
  One of Semiconductors' factories now uses C_4F_8O, but this gas is not yet officially in the PFC 'basket'. From 2006 there will be a new World Semiconductors template in which C_4F_8O is included and conversion factors will be updated. At the time of this report there are no known values for the GWP about this gas, so we report it as kilograms, under hazardous substances.
- The conversion factors used for direct energy and restricted substances will be updated and included in the software and the reporting manual in 2006.

Completeness

All 141 reporting organizations reported on time, except:

- Jilin, Semiconductors, and Queretero, Lighting (full year data not complete therefore not validated),
- Ledgewood (data completed after deadline).

The influence of the missing data on divisional and corporate level is negligible.

Comparability

- Relative reductions or increases are calculated using a production index that reflects production fluctuations. A suitable choice of production index is therefore a prerequisite for comparable changes, but is not always applicable across all types of reporting organizations or all types of parameters, even within one product division.
- The software tool for calculating the Global Warming Potential of PFC gases has been adapted slightly to align with the Tier 2C Method of the World Semiconductors Council, and the 2004 data has been modified accordingly. PFC data in the years 2001 to 2003 have not been modified because of non-availability of detailed information.

Health and safety reporting

Reporting standards

All reporting instructions, including definitions, procedures, calculation methods, etc. are available on our website.

Basis for reporting

Data are reported on a monthly basis and validated on a quarterly basis.

Accounting for organizational change

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 and internal control procedures. The definitions need improvement because some organizations are used to report according to local definitions.

Completeness

- Data reported over 2005 cover 88% 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 just over 7,000 FTEs.
  - Non-reporting of reporting units in the Netherlands accounting for more than 4.500 FTEs.
  - Non-validated reporting units in Turnhout (Belgium), accounting for just over 2.000 FTEs.
  - The remainder of the non-reported FTEs are divided over smaller units.

Comparability

In 2005 we used the same definitions as in 2004. In 2004 the Lost Work Time and Lost Workday Injury rate was likely to be lower than actual. Since we made further progress in enhancing the quality of internal control procedures it is likely that under-reporting will have decreased.

www.philips.com/sustainability/report

Overview Green Flagships 2005

Better environmental performance than chosen reference on Green Focal Areas (GFAs)

PD	Product group	Product type number	Energy	Packaging	Hazardous substances	Weight	Recycling & disposal	Lifetime	Notes
CE	19″ LCD Monitor	190S6	●			●		n/a	
	32″ CRT TV	32PW6420	●	●				n/a	
	32″ LCD TV	Philips 32PF9830	●				●	n/a	
	32″ LCD TV	32PF5320	●	●		●		n/a	
	37″ LCD TV	37PF7320A	●	●		●	●	n/a	1
	DECT phone	DECT 525	●	●		●	●	n/a	
	DECT phone	DECT 521	●			●		n/a	
	Digital AV Receiver System	DFR9000	●			●		n/a	
	Digital Satellite Receiver	DSR2010	●					n/a	2
	Digital Terrestrial Receivers	DTR4610	●	●		●	●	n/a	
	Digital Terrestrial Receivers	DTR2520	●	●		●		n/a	
	Micro Audio Jukebox	HDD084	●			●		n/a	
	Micro Audio Jukebox	HDD1620	●			●		n/a	
	Micro HiFi System	MCD280	●			●		n/a	
	Mobile phone	Xenium 9@98	●	●				n/a	
	Mobile phone	162	●	●				n/a	
Lighting	Component	Starters S2, S10			●			●	3
	Fluorescent lamp	MASTER TLD Xtra Polar			●			●	1
	Fluorescent lamp	MASTER TLD Xtreme Polar			●			●	1
	Fluorescent lamp	TL-D 80 Colours			●			●	
	Fluorescent lamp	T5 80 Colours			●			●	
	Lighting Electronics	HID PV C 50 & 100/S SDW-TG	●		●	●			3
	Lamp	PL-C 4 pin			●			●	
	Lamp	PL-C 2 pin			●			●	
	Lamp	PL-T 4 pin			●			●	
	Lamp	PL-T 2 pin			●			●	
	Lamp	PL-L			●			●	
	Lamp	EL-S R30 (dimmable)	●	●	●			●	
	Lamp	PL-TOP 4 pin			●			●	
	Lamp	PL-TOP 2 pin			●			●	
	Lamp	PL-L POLAR			●			●	
	Lamp	Cleo Consistancy	●					●	
	Lamp	Master Traffic	●					●	
	Lighting system	Mini Master colour 20W Non-Integrated	●					●	3
	Lighting system	Green Vision 1000W		●	●				
	Lighting system	ALTO Energy Advantage 25W System	●					●	3
	Lighting system	UHP E19.8 (TSP1)	●	●				●	3
	Luminaire	Koffer 2	●	●		●		●	
	Luminaire	City Vision III	●	●				●	
	Reflector lamp	Mini Master colour 25W PAR38	●					●	3
SC	AM/FM world receiver single chip car radio IC	TEF6901H	●	●				n/a	
	Antenna for DVB-T reception in portable TV applications	ANT2216	●			●	●	n/a	1
	Audio amplifier	Discrete Class D High Power Audio Amplifier	●	●		●		n/a	
	Mobile Phone RF front-end module	BGY504	●	●		●		n/a	
PMS	Defibrillator	HeartStart FRx				●		n/a	2
	Hardware platform for X-Ray analysis	PCR Eleva	●	●		●		n/a	
	Medical LCD monitor	MML 1821- PCR	●	●				n/a	
	Open MR system	Panorama 1.0T	●			●		n/a	1
POS	Optical pick-up unit	OPU6643		●	●			n/a	
DAP	Solarium	Innergize HB935	●			●		n/a	4

[1] Benchmarked against only one competitor as no other competitors offer products with comparable functionality

[2] Better performance than chosen reference on one Green Focal Area and Life Cycle Score (in accordance with definition)

[3] Milestone 1 passed in 2004, launched in 2005

[4] Product is launched in 2004

Global Reporting Initiative (GRI) Guidelines – General

Vision and strategy

	Indicator number		Page/s	Remark
	1.1	Statement of the organization's vision and strategy regarding sustainable development	7-9, 16-17, 18-25	
	1.2	Statement from the CEO describing key elements of the report	7-9	
Profile				
Organizational profile	2.1	Name of reporting organization	cover	
	2.2	Major products and/or services, including brands if appropriate	12	
	2.3	Operational structure of the organization	12	
	2.4	Description of major divisions, operating companies, subsidiaries and joint ventures	12	
	2.5	Countries in which the organization's operations are located	11	
	2.6	Nature of ownership; legal form		See *Philips Annual Report 2005*
	2.7	Nature of markets served	8, 12, 20-25, 28	
	2.8	Scale of the reporting organization	11-12	
	2.9	List of stakeholders, key attributes of each, and relationship to the reporting organization	26-27	
Report scope	2.10	Contact person(s) for the report, including e-mail and web addresses	4, 5, 82	
	2.11	Reporting period	cover, 4	
	2.12	Date of previous report	4	
	2.13	Boundaries of report (countries/regions, products/services, etc.) and any specific limitations	4, 74	
	2.14	Significant changes in size, structure, ownership	12, 74	
	2.15	Basis for reporting on joint ventures etc. affecting comparability from period to period	4	
	2.16	Explanation/nature of any re-statements of earlier reports (e.g. mergers/acquisitions)	74	
Report profile	2.17	Decisions not to apply GRI principles/protocols in the preparation of the report		Noted in this column
	2.18	Criteria/definitions used in accounting for cost/benefits	4	
	2.19	Significant changes in measurement methods	74	
	2.20	Policy and internal practices to enhance accuracy, completeness and reliability	38, 74	
	2.21	Policy and current practice on independent assurance	4, 72	
	2.22	Means by which report users can obtain additional information	4, 5, 82	

Governance structure and management systems

	Indicator number		Page/s	Remark
Structure and governance	3.1	Governance structure of the organization (including major committees)	12	
	3.2	Percentage of the Board of Directors (Supervisory Board) that are independent/non-executive directors		See *Philips Annual Report 2005*
	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	13-15, 16-17	
	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	13-15	
	3.7	Mission/values/codes of conduct/principles and status of implementation	13-15, 18-19	
	3.8	Mechanisms for shareholders to provide recommendations to Board of Management	13	
Stakeholder engagement	3.9	Basis for identification and selection of major stakeholders	26-27	
	3.10	Approaches to stakeholder consultation in terms of frequency of consultations by type	24-35	
	3.11	Type of information generated by stakeholder consultations	24-35	
	3.12	Use of information resulting from stakeholder engagements	24-35	
Overarching policies and management systems	3.13	Explanation of how the precautionary principle is addressed by the organization's policies	3, 13	
	3.14	Subscription to externally developed/voluntary charters/principles/initiatives	59	
	3.15	Principal industry and business association membership	17	
	3.16	Policies/systems for supply chain management and product stewardship	47-57, 61, 68-70	
	3.17	Approach to managing indirect impacts resulting from activities	47-61	
	3.18	Major decisions regarding locations or changes of operations	38, 40-41	
	3.19	Programs and procedures for improvement programs/actions	26-27, 33, 35, 38-39, 46-57, 61	
	3.20	Status of certification of environmental, labor, social accountability management systems	58	

Global Reporting Initiative (GRI) Guidelines – Core Indicators

Economic performance indicators

	Indicator number		Page/s	Remark
Customers	EC1	Net sales	11, 62	
	EC2	Geographic breakdown of key markets	63	
Suppliers	EC3	Cost of all goods, materials and services purchased	64, 68-69	
	EC4	Percentage of contracts paid in accordance with agreed terms		Under investigation
Employees	EC5	Total payroll and benefits broken down by country/region	64	
Providers of capital	EC6	Distribution to providers of capital broken down by interest/dividends on all classes of shares	65	
	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	42-45	

Environmental performance indicators

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	52, 58	
	EN4	Indirect energy use	52, 58	
Water	EN5	Total water use	52, 60	
Biodiversity	EN6	Location and size of land owned, leased or managed in biodiveristy-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	11, 46-48, 59	
	EN9	Use and emissions of ozone-depleting substances	49-50, 52-60	
	EN10	NO_x, SO_x and other significant air emissions by type	53, 60	
	EN11	Total amount of waste by type and destination	52, 59	
	EN12	Significant discharges to water by type	52, 53, 60	
	EN13	Significant spills of chemicals/oils/fuels in terms of total number and total volume	61	
Products and services	EN14	Significant environmental impact of principal products and services	54-57, 75	
	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	61	

Social performance indicators Labor practices and decent work

	Indicator number		Page/s	Remark
Employment	LA1	Geographical breakdown of workforce, where possible by region/country/status	40-41	
	LA2	Net employment creation and average turnover segmented per region/country	40-41	
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)	38	
Health & Safety	LA5	Practices on recording/notification of occupational accidents/diseases (relation to ILO)	38-39	
	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	38-39	
	LA8	Description of policies or programs (for the workplace and beyond) on HIV/AIDS	7, 43	
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	36-37	
	LA11	Composition of senior management and corporate governance bodies (including board of directors)	12, 36	
Human rights				
Strategy and management	HR1	Description of policies, corporate structure on human rights and monitoring mechanism and results	7, 13-15	
	HR2	Evidence of consideration of human rights (investment/procurement/suppliers/contractors)	69-70	
	HR3	Description of policy on human rights for supply chain and contractors; monitoring systems/results	69-70	
Non-discrimination	HR4	Description of global policies preventing all forms of discrimination and monitoring systems/results	13-15, 69-70	
Freedom of association/ collective bargaining	HR5	Description of policies on freedom of association and programs		www.philips.com/gbp
Child Labor	HR6	Description of policy excluding child labor, monitoring systems and results		www.philips.com/gbp
Forced and compulsory labor	HR7	Description of policies on forced and compulsory labor, monitoring systems and results		www.philips.com/gbp
Society				
Community	SO1	Description of policy on community impact, programs and monitoring systems and results	42-45	
Bribery and corruption	SO2	Description of policy on bribery and corruption, and compliance mechanisms		www.philips.com/gbp
Political contributions	SO3	Description of policy for managing political and lobbying contributions, and compliance mechanisms		www.philips.com/gbp
Product responsibility				
Customer health and safety	PR1	Description of policy on customer health and safety through products and services, and results	33	
Products and services	PR2	Description of policy on product information and labeling, and compliance mechanisms	33	
Respect for privacy	PR3	Description of policy and management system for consumer privacy, and compliance mechanisms	15	

Glossary

CFC	Chlorofluorocarbon CFCs are considered deleterious to the ozone layer.
CHC	Chlorohydrocarbon
CO_2	Carbon dioxide This is the most prevalent greenhouse gas.
Environmental Management System	That part of an organization's general mangement 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 10^9 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.
GRI	Global Reporting Initiative
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 Indicators
NGO	Non-governmental organization
NO_X	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 indicatin 10^{15} times base unit (1 followed by 15 zeroes).
SO_X	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 Bruntland, 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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