PHILIPS

International Financial Reporting Standards (IFRS)

Impact on the 2004 consolidated financial statements of Royal Philips Electronics

March 29, 2005

Content

- Introduction

- Main accounting differences and impact

- 2004 financial statements in accordance with IFRS

Note: all amounts in millions of euros | The data included in this report are unaudited

Introduction

- In 2002 Philips adopted US GAAP as primary accounting standards
- To meet Dutch legal requirements the Company reconciles from US GAAP into Dutch GAAP and provides this additional information in the annual report
- The most important considerations to introduce US GAAP were comparability with the relevant peer group and the desire to communicate in the language that is best understood in the global capital markets

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The peer group when US GAAP was adopted

Company	Primary GAAP	Company	Primary GAAP
Electrolux AB	Sweden	Nokia	IAS
Emerson Electric	US	Samsung	Korean
Ericsson	Sweden	Sanyo	US
Flextronics	US	Sharp	Japan
Hitachi	US	Siemens	US until 2007
Kyocera	US	Sony	US
LG Electronics	Korean	Toshiba	US
Matsushita	US	Tyco Intl Ltd	US
Mitsubishi	Japan	Whirlpool Corp	US
NEC Corp	US		

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Financial reporting as of 2005

- To continue comparability, both with the peer group and over time, Philips will maintain US GAAP as primary accounting standard
- Additional IFRS information will be provided as supplemental information in the annual report and will include full consolidated statements of income and cash flow as well as a consolidated balance sheet and relevant notes
- In the quarterly reports a reconciliation of net income and equity in accordance with IFRS will be provided as supplementary information, together with a condensed consolidated balance sheet and income statement in accordance with IFRS

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The main accounting differences affecting Philips relate to:

- Product development expenses
- Goodwill
- Pensions and other postretirement benefits
- Leasing
- Unconsolidated companies
- Other differences in income
- Taxation

PM: Because Philips already accounts for derivatives in accordance with SFAS 133 and expenses share-based payments as permitted by SFAS 123 these items cause no significant differences

Product development expenses (1)

- Whereas US GAAP requires that all research and development costs are immediately expensed IFRS requires capitalization of qualifying expenses as an intangible asset and subsequent amortization.

- Capitalization is required when the Company can demonstrate:
  - Technical feasibility of completing the asset
  - The intention to complete, use or sell the asset
  - The ability to use or sell the asset
  - How the asset will generate economic benefits
  - Availability of adequate resources to complete the asset
  - The ability to measure expenditure reliably

Product development expenses (2)

- Research costs can never be capitalized. Certain development costs do not qualify for capitalization because they do not meet all of the conditions mentioned previously

Impact for Philips

- Opening balance sheet 1.1.2004: recognition of an asset of EUR 1,232 million (increase of equity)
- In 2004: Capitalization of new expenditures for EUR 639 million and amortization of development assets for EUR 420 million
- Closing balance at 31.12 2004: EUR 1,442 million (impacted by currency translation differences)

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Goodwill

- Both IFRS and US GAAP require capitalization of goodwill with impairment testing and prohibit amortization
- This system is applied since 2002 in the US GAAP accounts but can only be applied from 2004 onwards for IFRS

Impact for Philips

- Opening balance sheet 1.1.2004: Reduction of goodwill as a result of two more years of amortization for EUR 395 million (decrease of equity)
- Ongoing: No change except for currency translation differences and lower goodwill impairment charges in case these would arise

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Pensions and other postretirement benefits (1)

- Philips applies FAS 87 for pension accounting which is substantially the same as the IFRS standard for pension accounting
- Differences arise because,a.o. IFRS 1, “First time adoption” allows recognition of cumulative actuarial gains and losses at the date of transition to IFRS in equity. Furthermore the so called additional minimum pension liabilities recognized under US GAAP do not exist in IFRS

Impact for Philips

- Opening balance sheet 1.1.2004: Reduction of equity EUR 1,497 million
- In 2004: Lower pension and related charges of EUR 369 million for IFRS
- Closing balance at 31.12.2004: Reduction of equity of EUR 956 million

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Pensions and other postretirement benefits (2)

- IFRS has stricter rules than US GAAP for the recognition of prepaid pension assets. IAS 19 requires that a prepaid asset is only recognized when and to the extent that the present value of future premium discounts or refunds exceeds the book value of the prepaid asset
- For the Dutch Pensionfund the consequence could be that an asset can only be recognized when and to the extent that the capital adequacy threshold of the "Pensioen- en Verzekeringskamer" is met. The interpretation committee of the IASB (IFRC) has been asked for a final conclusion on the issue. As long as this final conclusion is not available we assume that the prepaid asset can not be recognized to the extent that the threshold is not met

Impact for Philips

- Opening balance sheet 1.1.2004: lower prepaid assets of EUR 227 million (reduction of equity)
- In 2004: Higher pension charges due to additional prepayments of EUR 518 million
- Closing balance at 31.12.2004: lower prepaid assets of EUR 745 million

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Leasing (1)

- The most important difference relates to the recognition of profit on operational sale- and lease back transactions
- US GAAP requires amortization over the life of the lease for such profits, IFRS requires up-front recognition when the sale is at market conditions

Impact for Philips

- Opening balance sheet 1.1.2004: Increase of equity EUR 107 million
- In 2004: Lower IFRS income for existing leases of EUR 5 million
- Closing balance at 31.12 2004: EUR 102 million

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Leasing (2)

- In some cases operating leases under US GAAP do not qualify as such for IFRS and will be recognized on the balance sheet. This has a limited impact for Philips and does not change equity or net income

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Unconsolidated companies

- Unconsolidated companies that are accounted for in accordance with the equity method can face differences similar to those discussed before that impact their valuation in the Philips (IFRS) books
- IFRS requires an additional charge to equity for goodwill amortization of EUR 244 million as of 31.12.2004 (EUR 255 million as of 1.1.2004)
- IFRS requires reversal of asset impairments in case the reasons for the impairment no longer exist. US GAAP prohibits such reversals. Some unconsolidated companies have recognized asset impairments in the past that require reversal for IFRS with a corresponding increase of equity. This results in an increase of equity of EUR 17 million as of 31.12.2004 (EUR 24 million as of 1.1.2004)
- Pension accounting results in differences that are similar to those discussed before but have a limited impact (EUR 3 million reduction of equity, both opening and closing balance sheet)

Other differences in income

- IFRS requires the reversal of previously recognized impairment charges in case the reason for the impairment no longer exists whereas US GAAP prohibits such reversals. Prior to 2004 Philips recognized impairment charges on investments in available for sale securities (a.o. Vivendi Universal and Great Nordic) and on investments in certain unconsolidated companies that require reversal for IFRS accounting purposes. As a consequence the result on disposal of such investments is different in the IFRS accounts. For these items differences in equity do not arise because revaluations subsequent to the impairment are credited to stockholder equity under both IFRS and US GAAP.

Impact for Philips

- Lower IFRS income on sale of securities EUR 202 million
  (reported in financial income and expenses)
- Higher IFRS income due to reversal of security impairments EUR 19
  (reported in financial income and expenses)

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Taxation

- Most differences discussed before are impacted by income taxes and therefore reduce/increase deferred income taxes for Philips

Impact for Philips

- Opening balance sheet 1.1.2004: Higher tax assets of EUR 201 million (net of liabilities,increase of equity)
- In 2004: Higher IFRS net income of EUR 4 million due to tax differences
- Closing balance at 31.12.2004: Higher tax assets of EUR 123 million (net of liabilities)

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Impact on equity

	1.1.2004	31.12.2004
Stockholders' equity under US GAAP	12,763	14,860
Capitalization of development costs	1,232	1,442
Pensions and other postretirement benefits	(1,724)	(1,701)
Goodwill amortization	(395)	(355)
Unconsolidated companies	(234)	(230)
Recognized results on sale and lease back transactions	107	102
Deferred tax effect	201	123
Others	(3)	(2)
Total adjustments	(816)	(621)
Stockholders' equity under IFRS	11,947	14,239

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Reconciliation of net income

US GAAP net income	2,836
Capitalization development costs	639
Amortization of development assets	(420)
Pensions and other postretirement benefits	(149)
Gain on sale of Vivendi Universal shares	(202)
Reversal of prior impairment Great Nordic shares	19
Results unconsolidated companies	34
Higher dilution gain on partial disposal of NAVTEQ	19
Income taxes	4
Others	3
Total adjustment	(53)
IFRS net income	2,783

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Financial Statements in accordance with IFRS for 2004

Consolidated balance sheet in accordance with IFRS

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Consolidated balance sheet	December 31, 2003		December 31, 2004	
	IFRS	US GAAP	IFRS	US GAAP
Current assets:				
Cash and cash equivalents	3,072	3,072	4,349	4,349
Receivables	4,628	4,628	4,528	4,528
Inventories	3,204	3,204	3,230	3,230
Other current assets	653	1,010	883	1,216
Total current assets	**11,557**	**11,914**	**12,990**	**13,323**
Non-current assets:				
Investments in unconsolidated companies	4,607	4,841	5,441	5,670
Other non-current financial assets	1,213	1,213	876	876
Non-current receivables	218	218	227	227
Other non-current assets	2,139	2,581	2,122	2,823
Property, plant and equipment	4,916	4,879	5,028	4,997
Intangible assets excluding goodwill	2,367	1,271	2,324	989
Goodwill	2,099	2,494	1,463	1,818
Total assets	**29,116**	**29,411**	**30,471**	**30,723**
Current liabilities:				
Accounts and notes payable	3,205	3,205	3,499	3,499
Accrued liabilities	3,088	3,165	3,231	3,307
Short-term provisions	1,131	949	976	781
Other current liabilities	649	649	627	627
Short-term debt	1,861	1,860	962	961
Total current liabilities	**9,934**	**9,828**	**9,295**	**9,175**
Non-current liabilities:				
Long-term debt	4,053	4,016	3,583	3,552
Long-term provisions	2,175	1,976	2,237	2,117
Other non-current liabilities	832	653	832	736
Total liabilities	**16,994**	**16,473**	**15,947**	**15,580**
Minority interests	175	175	285	283
Stockholders' equity	11,947	12,763	14,239	14,860
Total liabilities and equity	**29,116**	**29,411**	**30,471**	**30,723**
Number of common shares outstanding at the end of period (in thousands)	1,280,686	1,280,686	1,281,527	1,281,527
Ratios				
Stockholders' equity,	11,947	12,763	14,239	14,860
per common share in euros	9.33	9.97	11.11	11.60
Inventories as a % of sales	11.0	11.0	10.7	10.7
Net debt : group equity ratio	19 : 81	18 : 82	1 : 99	1 : 99

Consolidated statements of income in accordance with IFRS

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	January to December 2004	
	IFRS	US GAAP
Sales	30,319	30,319
Cost of sales	(20,186)	(20,155)
Gross margin	10,133	10,164
Selling expenses	(4,528)	(4,520)
General and administrative expenses	(1,423)	(1,332)
Research and development expenses	(2,332)	(2,534)
Impairment of goodwill	(591)	(596)
Restructuring and asset impairments	(288)	(288)
Other business income (expense)	729	713
Income from operations	1,700	1,607
Financial income and expenses	34	216
Income before taxes	1,734	1,823
Income tax expense	(354)	(358)
Income after taxes	1,380	1,465
Results relating to unconsolidated companies including net dilution results	1,456	1,422
Minority interests	(53)	(51)
Net income	2,783	2,836
Income from operations as a % of sales	5.6	5.3
Weighted average number of common shares outstanding (after deduction of treasury stock) at the end of the period (in thousands):	1,280,251	1,280,251
Basic earnings per common share in euros:	2.17	2.22

Consolidated balance sheet in accordance with IFRS

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Consolidated balance sheet	1st quarter		2nd quarter		3rd quarter		4th quarter	
	IFRS	US GAAP	IFRS	US GAAP	IFRS	US GAAP	IFRS	US GAAP
Current assets:								
Cash and cash equivalents	3,105	3,105	2,434	2,434	1,610	1,610	4,349	4,349
Receivables	4,868	4,868	4,863	4,863	5,215	5,215	4,528	4,528
Inventories	3,543	3,543	3,738	3,738	4,055	4,055	3,230	3,230
Other current assets	492	1,004	518	1,050	497	985	883	1,216
Total current assets	**12,008**	**12,520**	**11,553**	**12,085**	**11,377**	**11,865**	**12,990**	**13,323**
Non-current assets:								
Investments in unconsolidated companies	5,250	5,506	5,651	5,910	6,305	6,545	5,441	5,670
Other non-current financial assets	1,322	1,322	1,316	1,316	1,210	1,210	876	876
Non-current receivables	227	227	252	252	241	241	227	227
Other non-current assets	2,114	2,450	2,115	2,492	1,974	2,451	2,122	2,823
Property, plant and equipment	5,450	5,413	5,429	5,394	5,290	5,255	5,028	4,997
Intangible assets excluding goodwill	2,401	1,255	2,380	1,192	2,358	1,129	2,324	989
Goodwill	2,189	2,591	2,178	2,581	2,196	2,591	1,463	1,818
Total assets	**30,961**	**31,284**	**30,874**	**31,222**	**30,951**	**31,287**	**30,471**	**30,723**
Current liabilities:								
Accounts and notes payable	3,206	3,206	3,362	3,362	3,456	3,456	3,499	3,499
Accrued liabilities	3,325	3,399	3,077	3,163	3,278	3,359	3,231	3,307
Short-term provisions	1,059	863	1,050	884	1,066	918	976	781
Other current liabilities	744	744	646	646	717	717	627	627
Dividend payable	460	460	0	0	0	0	0	0
Short-term debt	2,009	2,008	2,128	2,127	1,171	1,170	962	961
Total current liabilities	**10,803**	**10,680**	**10,263**	**10,182**	**9,688**	**9,620**	**9,295**	**9,175**
Non-current liabilities:								
Long-term debt	4,167	4,131	4,054	4,019	3,687	3,654	3,583	3,552
Long-term provisions	2,328	2,131	2,231	2,014	2,241	2,010	2,237	2,117
Other non-current liabilities	926	742	913	736	885	716	832	736
Total liabilities	**18,224**	**17,684**	**17,461**	**16,951**	**16,501**	**16,000**	**15,947**	**15,580**
Minority interests	314	314	327	327	315	315	285	283
Stockholders' equity	12,423	13,286	13,086	13,944	14,135	14,972	14,239	14,860
Total liabilities and equity	**30,961**	**31,284**	**30,874**	**31,222**	**30,951**	**31,287**	**30,471**	**30,723**
Number of common shares outstanding at the end of period (in thousands)	1,279,125	1,279,125	1,279,958	1,279,958	1,280,391	1,280,391	1,281,527	1,281,527
Ratios								
Stockholders' equity,	12,423	13,286	13,086	13,944	14,135	14,972	14,239	14,860
per common share in euros	9.71	10.39	10.22	10.89	11.04	11.69	11.11	11.60
Inventories as a % of sales	12.1	12.1	12.5	12.5	13.4	13.4	10.7	10.7
Net debt : group equity ratio	19 : 81	18 : 82	22 : 78	21 : 79	18 : 82	17 : 83	1 : 99	1 : 99

Consolidated statements of income in accordance with IFRS

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	1st quarter		2nd quarter		3rd quarter		4th quarter	
	IFRS	US GAAP	IFRS	US GAAP	IFRS	US GAAP	IFRS	US GAAP
Sales	6,631	6,631	7,280	7,280	7,229	7,229	9,179	9,179
Cost of sales	(4,447)	(4,438)	(4,851)	(4,842)	(4,826)	(4,817)	(6,062)	(6,058)
Gross margin	2,184	2,193	2,429	2,438	2,403	2,412	3,117	3,121
Selling expenses	(1,007)	(1,005)	(1,089)	(1,087)	(1,085)	(1,084)	(1,347)	(1,344)
General and administrative expenses	(387)	(361)	(357)	(331)	(352)	(326)	(327)	(314)
Research and development expenses	(569)	(614)	(615)	(654)	(605)	(641)	(543)	(625)
Impairment of goodwill	-	-	(14)	(14)	(2)	(4)	(575)	(578)
Restructuring and asset impairments	(16)	(16)	(36)	(36)	(58)	(58)	(178)	(178)
Other business income (expense)	18	21	51	40	732	720	(72)	(68)
Income from operations	223	218	369	356	1,033	1,019	75	14
Financial income and expenses	(66)	(66)	(65)	(65)	(70)	(70)	235	417
Income before taxes	157	152	304	291	963	949	310	431
Income tax (expense) benefit	(48)	(46)	(91)	(87)	(101)	(97)	(114)	(128)
Income after taxes	109	106	213	204	862	852	196	303
Results relating to unconsolidated companies including net dilution results	451	457	424	430	399	337	182	198
Minority interests	(13)	(13)	(18)	(18)	(17)	(17)	(5)	(3)
Net income	547	550	619	616	1,244	1,172	373	498
Income from operations as a % of sales	3.4	3.3	5.1	4.9	14.3	14.1	0.8	0.2
Weighted average number of common shares outstanding (after deduction of treasury stock) at the end of the period (in thousands):	1,280,770	1,280,770	1,280,034	1,280,034	1,280,091	1,280,091	1,280,251	1,280,251
Basic earnings per common share in euros:	0.43	0.43	0.48	0.48	0.97	0.92	0.29	0.39

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