

PHILIPS

International Financial Reporting Standards (IFRS) impact for Philips

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Financial Analysts Day 2004

Agenda

- Introduction
- Main accounting differences and impact
- Future reporting

Introduction

- In 2002 Philips adopted US GAAP as it's primary accounting standard
- 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

The peer group when US GAAP was adopted

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

Financial reporting as of 2005

- To continue comparability, both with the peer group and over time, the Company 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
- On a quarterly basis income and equity in accordance with IFRS will be provided as supplementary information

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The main accounting differences affecting Philips are related to:

- Development expenses
- Goodwill accounting
- Pensions
- Lease accounting
- Taxation
- The same differences apply to the unconsolidated subsidiaries

p.m. Because Philips already accounts for derivatives in accordance with SFAS 133 there are no significant differences in this area

Development costs (1)

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

Development costs (2)

- Research costs can never be capitalized and certain Development costs will not qualify for capitalization because they do not meet all of the conditions mentioned previously
- Impact for Philips:
 - Opening balance sheet: recognition of an asset of approx. EUR 1.5 billion (increase of equity)
 - Ongoing: Capitalization of new expenditures and amortization of the asset → limited effect on income

Goodwill accounting

- Both IFRS and US GAAP require capitalization of goodwill with impairment testing and prohibit amortization
- This 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: Reduction of goodwill as a result of two more years of amortization for approx. EUR 0.4 billion (decrease of equity)
 - Ongoing: No impact (except for lower goodwill impairment charges in case these would arise)

Pension accounting (1)

- Philips applies FAS 87 for pension accounting which is substantially the same as the IFRS standard for pension accounting
- Still a difference arises because IFRS 1, “First time adoption” requires recognition of cumulative actuarial gains and losses at the date of transition to IFRS in equity
- Impact for Philips
 - Opening balance sheet: Reduction of equity EUR 1.5 billion
 - Ongoing: Lower pension charges because amortization of these cumulative actuarial gains and losses is not required for IFRS

Pension accounting (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. Final agreement on this interpretation is pending. We currently assume that the prepaid asset can not be recognized
- Impact for Philips
 - Opening balance sheet: Reduction of equity EUR 0.25 billion
 - Ongoing: Higher pension charges in case of prepayments until capital adequacy threshold in the Netherlands is met

Lease accounting

- Difference relates to the recognition of profit on 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: Increase of equity EUR 0.1 billion
 - Ongoing: Lower IFRS income for existing leases in accordance with amortization under US GAAP

p.m. In some cases operating leases under US GAAP may not qualify as such for IFRS and will be recognized in the balance sheet. This will not have a significant impact for Philips

Taxation

- Most differences are affected by income tax and will therefore reduce/increase deferred income taxes for the Company
- Impact for Philips:
 - Opening balance sheet: Increase of equity EUR 0.05 billion
 - Ongoing: Depending on composition of differences

Unconsolidated companies

- Unconsolidated companies (equity method valued) face similar differences that will impact their valuation in the Philips (IFRS) books. This will lead to an additional charge to equity for goodwill amortization (0.3 billion).
- 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 may require reversal for IFRS with a corresponding increase of equity (amount still under review, for consolidated entities it has been determined that such reversals are not required)

Summary (equity impact)

	Equity impact	Ongoing
Capitalization development expense	1.5	Limited
Additional goodwill amortization	(0.4)	None
Recognition of cum. actuarial gains and losses	(1.5)	Lower costs
Reduction prepaid pension assets	(0.25)	None or Higher costs
Changes in deferred result sale and lease back	0.1	Limited
Change in deferred tax	0.05	Related to items above
Changes in UCCs	p.m.	

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Future reporting

- Detailed explanation of IFRS impact in Annual Report 2004
- Publication 2004 IFRS re-statement on IR internet in Q1 2005
- Quarterly earnings announcements with supplementary IFRS income and equity information starting April 18, 2005
- Annual report 2005 will be based on US GAAP with IFRS financial statements as supplemental information (and additional IFRS disclosures where required)

Financial reporting will be accelerated in 2005

- Annual results 2004
 - January 27, 2005
Q4 press release
Management Report 2004, a condensed version of the Annual Report
 - February 22, 2005
Full Annual Report 2004
- Quarterly press releases 2005
 - Monday April 18, 2005 Q1
 - Monday July 18, 2005 Q2
 - Monday October 17, 2005 Q3

