

Supplier Sustainability Involvement Program

The Philips Supplier Sustainability Involvement Program is built on five pillars: create commitment by setting out our requirements; getting suppliers to understand our requirements and monitoring identified risk suppliers through audits; working with suppliers to resolve issues; and engaging stakeholders.

| 1. Create commitment | 2. Build understanding | 3. Monitor identified risk suppliers | 4. Manage risk | 5. Work with stakeholders |
|------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> • Supplier Sustainability Declaration • Regulated Substances List | <ul style="list-style-type: none"> • Training and capability building | <ul style="list-style-type: none"> • Philips risk assesment • EICC audit tool | <ul style="list-style-type: none"> • Follow up • Consequence management • Repeat audit cycle every 3 years | <ul style="list-style-type: none"> • Transparency • Constructive dialog |

Figure 1: Philips Supplier Sustainability Involvement Program

Building block 1: Create commitment

In 2009 we updated the Philips Supplier Sustainability Declaration in accordance with the updated EICC Code of Conduct, while maintaining the Philips appendix with stricter requirements on freedom of association/collective bargaining. This is in keeping with our General Business Principles. Where freedom of association/collective bargaining is restricted by law, we look to see if there are other means of open communication between the supplier's management and workers. Our Supplier Sustainability Declaration is an integral part of our general purchasing agreements with suppliers, and covers the areas of labor, health and safety, environment, management systems and ethics.

| Labor | Health & Safety | Environment | Management systems | Ethics | General |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> • Freely Chosen Employment • Child Labor Avoidance • Working Hours • Wages and Benefits • Humane Treatment • Non-Discrimination • Freedom of Association | <ul style="list-style-type: none"> • Occupational Safety • Emergency Preparedness and Response • Occupational Injury and Illness • Industrial Hygiene • Physically Demanding Work • Machine Safeguarding • Dormitory and Canteen | <ul style="list-style-type: none"> • Environmental Permits and Reporting • Pollution Prevention and Resource Reduction • Hazardous Substances • Wastewater and Solid Waste • Air Emissions • Product Content Restrictions | <ul style="list-style-type: none"> • Company Commitment • Management Accountability & Responsibility • Legal and Customer Requirements • Risk Assessment and Risk Management • Performance Objectives with Implementation Plan and Measures • Training • Communication • Worker Feedback and Participation • Audits and Assessments • Corrective Action Process • Documentation & Records | <ul style="list-style-type: none"> • Business Integrity • No Improper Advantage • Disclosure of Information • Protection of Intellectual Property • Fair Business, Advertising and Competition • Protection of Identity | <ul style="list-style-type: none"> • EICC Code • Compliance with the Law |

Figure 2: Scope of the Philips supplier sustainability declaration

Building block 2: Build understanding

In 2010 we organized eight training sessions in China, Brazil and Singapore for suppliers included in the 2010 audit plan. 489 supplier representatives attended the trainings.

Philips' supplier managers play an important role in the supplier sustainability process. Their direct involvement in the audit preparation and follow-up process emphasizes to our suppliers that sustainability is an integral part of working with Philips. To equip our supplier managers, supplier sustainability management is part of the purchasing core training curriculum, and 128 Philips supplier managers were trained in 2010 during 10 training sessions in Europe, the US and Asia.

In 2010 we included a sustainability rating in the Global Supplier Rating System to support supplier managers in further embedding sustainability in commercial decision making.

[Supplier sustainability declaration >](#)

[Regulated substances list >](#)

Building block 3: Monitor identified risk suppliers

Risk-based implementation / Identifying risk suppliers

Given the size and complexity of our supply chain we needed to focus our efforts, and developed an approach based on the supplier's risk profile related to spend, country of production, business risk and type of supplier relationship. Where risk is identified we train our suppliers in preparation for third-party audits. In 2010, we updated the risk country list based on latest versions of two Maplecroft indices: Legal and Regulatory Environment Index and the Human Rights Index. Countries that score high or extreme high risk are included in the Philips Risk Country List 2010. 76 countries are on the risk list, amongst others a number of countries in which we source: China, India, Brazil, Mexico, Vietnam, Indonesia, Thailand, Pakistan, Philippines, Belarus, Russia, and Ukraine.

Our suppliers



Sustainability audits 2010 done in:

| | |
|-----------|-------------|
| Brazil | Mexico |
| China | Philippines |
| India | Ukraine |
| Indonesia | Vietnam |

Spend per region:

| | |
|---------------|-----|
| EMEA | 45% |
| Asia Pacific | 33% |
| North America | 17% |
| South America | 5% |

Top 5 Purchasing Countries:

China, including Hong Kong
 United States
 Germany
 Netherlands
 Japan

966 suppliers have been identified as risk suppliers, including 916 product and component suppliers and 50 service providers. All risk suppliers are by definition part of our audit program.

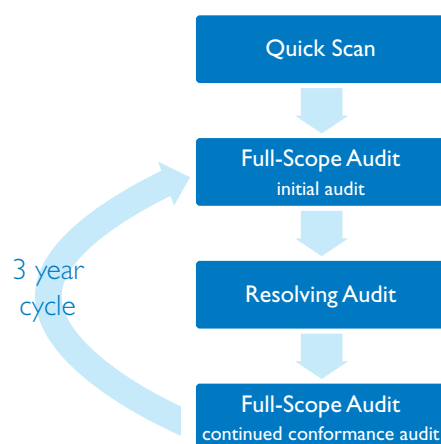


Figure 3: Audit cycle

For new suppliers this means that they need to demonstrate resolution of any zero-tolerance non-compliances before their first shipment to Philips. As part of the Philips integration process for acquisitions, risk suppliers from acquisitions are audited in line with Philips' supplier sustainability policy. All existing risk suppliers, including those from acquisitions, go through a full-scope audit every 3 years.

The Philips Supplier Sustainability audits are based on EICC tools to reduce duplication of efforts and to send a consistent message to suppliers. When we source from a supplier that also delivers to other EICC member companies, we aim to team up and jointly audit the supplier via the EICC Validated Audit Program.

The goal of the audit is to verify that a supplier works in accordance with the provisions in the Philips Supplier Sustainability Declaration, and if needed identify areas and ways for improvement. During this audit, the auditors cross-check data from multiple sources to ensure validity. Interviews with workers and senior management are a standard part of the audit, as well as a tour of the factory, dormitories and canteen, and a review of different records, policies and procedures. The audit typically takes 2 to 4 man-days on site, and covers the complete production facility and workers at all production lines. During the feedback session at the end of the audit good practices, areas for improvement and corrective actions are discussed between the auditors and the supplier.

Understanding of our compliance requirements is enhanced by a system of quick scans conducted prior to full scope audits to identify and correct critical issues. This is particularly valuable for new supply bases from acquisitions that have not been exposed to the EICC Code.

Full-scope audits outsourced

For reasons of independence, professionalism and capacity, we have implemented a policy that requires third parties to conduct initial and continual conformance audits. In 2010 all of these audits were performed by external auditing bodies (SGS and Bureau Veritas), completing the outsourcing process that we initiated in 2006.

We require our suppliers to pay for their third-party audits, believing this is an effective way of embedding EICC requirements in the supply chain, and have suppliers take ownership of their performance.

In that context, Philips will accept an alternative audit report from suppliers after a quality check. This is only possible when the alternative audit was done against a recognized and comparable (industry) standard, such as EICC, and executed by an independent audit body, further underlining the importance of industry-wide collaboration and outsourced auditing. The majority of our suppliers however indicated that they had not been audited before.

Updated Supplier Sustainability Audit Checklist

In 2009 we adopted the new EICC Code of Conduct and, as with the previous version, we added freedom of association and collective bargaining. We included it as a standard clause in all the purchasing contracts. EICC finalized the new audit checklist in December 2009 and in 2010 we started training and auditing suppliers based on the new code and checklist.

Main changes in new checklist:

- Around 40 new questions were added
- More questions on deployment of code to sub-contractors in the supply chain
- Stricter requirements and classification of labor topics like working hours, working days, minimum wages, overtime premiums and record keeping
- Additional questions on chemical composition of products and components, and questions on waste collection and recycling.

[Audit checklist >](#)

Building block 4: Manage risk

Resolving non-compliance with support of Philips sustainability experts

The resolving audits are usually done by a team of internal sustainability experts, and in some cases by an external audit body due to capacity restrictions. Since 75% of the audits take place in China, the majority of our experts are located there, followed by India and Brazil.

If areas of non-compliance were identified during the audits, the Philips supplier managers and sustainability experts will follow-up with the suppliers by means of resolving audits. Experts are available to support the supplier by sharing best practices, defining corrective action plans and monitoring the implementation. Most suppliers will be visited twice by the expert on-site. Experts will report progress to the purchasing organization and escalate issues like lack of progress or exceeding deadlines. Only after confirmation by either the Philips sustainability expert or an external audit body, will we consider an identified non-compliance as closed.

In most cases an on-site resolving audit is necessary to check implementation of the corrective action plan. When possible we will do a document check to confirm closure of the non-compliance, e.g. in case of permits or other documentation.

We work with standard deadlines to monitor a supplier's resolving process and escalate lack of progress. Where appropriate we will adjust this deadline based on the nature of the issues. Zero-tolerance non-compliances have a standard resolving deadline of 3 months, meaning that within 3 months of the full-scope audit date a resolving audit will take place to confirm closure of the non-compliance. For limited tolerance non-compliances the standard deadline is 6 months.

Building block 5: Work with stakeholders

A consistent message from multiple customers to suppliers is needed to leverage impact. Alignment can come from collaboration within the industry; participants benefit by sharing knowledge and resources, standardizing tools and processes, avoiding duplication of efforts, and developing consistent approaches. For Philips the most significant supply chain partnership is organized by the Electronic Industry Citizenship Coalition (EICC). The EICC member companies jointly develop tools to monitor and improve supply chain performance across the electronics sector.

IDH multi-stakeholder project

In 2010 we joined forces with frontrunner companies, civil society organizations and labor unions and set up the working group for the new electronics program of the Dutch Sustainable Trade Initiative (IDH). IDH's mission is the acceleration and up-scaling of social and ecological sustainability within mainstream commodity markets from emerging countries to the Netherlands and Western Europe. In this way, IDH is working on the Millennium Development Goals for poverty reduction, sustainable environment, and an open trading and financial system.

The IDH electronics program's goal is to contribute to improving the working conditions of 500,000 workers in the Pearl River delta in China. Its ambition is to explore new ways to engage local government, industry and workers and introduce more sustainable ways of operation. Good practices of frontrunner companies as well as civil society initiatives will be taken as a point of reference. The program expects to engage and influence local companies in different parts of the supply chain (multiple tiers) and will focus on specific needs of the involved suppliers related to the key themes: workplace health and safety, communication between workers and management, and environmental practices.

In 2010 we designed the building blocks for the program which is expected to be implemented in 2011. For more information, please visit the IDH site:

<http://www.dutchsustainabletrade.com/en/electronics>

Other stakeholder engagement activities

Engaging with relevant stakeholders helps us to improve our programs and shape our supplier sustainability vision 2015. 2010 engagement activities included:

- We initiated two stakeholder workshops in Eindhoven and Amsterdam with civil society organizations and labor unions to exchange views on ways to address the challenges in the electronics supply chain (participants: Amnesty, GoodElectronics, MakeITfair, FNV mondiaal, FNV bondgenoten, etc.)
- We met with Dutch politicians to discuss supply chain transparency and conflict minerals
- We contributed to the UN Global Compact guidance tool for Supply Chain Sustainability
- We continued our dialog with investors
- We financially sponsored the pilot of the tin organization ITRI to improve supply chain transparency for conflict minerals.

“The GoodElectronics Network welcomes the increasingly open and collaborative stance of Philips concerning genuine engagement with civil society stakeholders. For the coming year(s), GoodElectronics encourages Philips to go that extra mile, in working towards full compliance with international labor standards, in its own operations as well as throughout its supply chain. Significant progress can be made by engaging more with trade unions at the global level, and by practicing supply chain transparency.”

Pauline Overeem, GoodElectronics
International Network on Human Rights
& Sustainability in Electronics