



# CSR Report 2007

2006.04.01 – 2007.03.31

Kao Corporation



## Mission

Our mission is “to strive for the wholehearted satisfaction and enrichment of the lives of people globally” through the Company’s core domains of cleanliness, beauty, health, and chemicals.

Fully committed to this mission,  
all members of the Kao Group work together with passion to provide products and brands of excellent value created from the consumer/customer’s perspective.  
In so doing, we “share joy with the consumer/customer.”



### ***Yoki-Monozukuri***

We define *Yoki-Monozukuri* as “a strong commitment by all members to provide products and brands of excellent value for consumer satisfaction”. In Japanese, *Yoki* literally means “good/excellent”, *Monozukuri* means “development/manufacturing of products”.

As part of the steady and steadfast pursuit of its mission, the Kao Group presents this report on the CSR activities it is undertaking together with various stakeholders.

### Editorial Policy for CSR Report 2007

Kao began issuing its Environment, Safety and Health Report in 1998. In 2005, we augmented the content of that report to introduce our business activities from the perspective of Corporate Social Responsibility (CSR). We did that in an effort to disclose and provide information responding to the interests of a wide variety of stakeholders and began publishing a “CSR Report.”

This report is composed of three sections: The “CSR Management System” section addressing management fundamentals; the “Responsibilities to Stakeholders” section providing information on various initiatives; and the “Environmental Activities” section discussing progress and performance in protecting the environment.

In addition, to promote better understanding of *Yoki-Monozukuri* — CSR initiatives that are deeply rooted in our daily business activities — we have included feature reports covering business development and communicating the voices of internal and external stakeholders in our “Health Care Food Business” and our “Chemical Business.”

To enhance readability, we have begun this year to use a universal design font.

### Scope of Reporting

Organization covered:	Kao Corporation*. When information is provided on other organizations, the names of those organizations are noted in the text.
Period covered:	Performance data covers fiscal year 2006 (April 1, 2006 to March 31, 2007). Occupational safety data, however, is for calendar year 2006 (January 1, 2006 to December 31, 2006). Some information on fiscal year 2007 activities is also provided.
Independent review:	Kao's CSR Reports have undergone independent reviews since 2003. This year, the report was reviewed by the Tohatsu Environmental Research Institute Ltd.
Activities covered:	CSR activities related to the business activities described on Kao's web site ( <a href="http://www.kao.co.jp/en/company/fields/">http://www.kao.co.jp/en/company/fields/</a> ). Detailed data on economic performance is available in our Annual Report 2007.
Issuing period:	Issue date of the previous report: July 2006 Next scheduled issue of the report: July 2008
Guidelines referenced:	<ul style="list-style-type: none"> <li>• GRI 2002 Sustainability Reporting Guidelines</li> <li>• Environmental Reporting Guidelines (2003) and Environmental Accounting Guidelines (2005) by the Ministry of the Environment of Japan</li> <li>• Environmental Accounting Guidelines for Chemical Companies (November 2003) by the Japan Chemical Industry Association</li> </ul>

\*Offices: Kayabacho, Sumida, and Osaka; Plants: Sakata, Tochigi, Kashima, Tokyo, Kawasaki, Toyohashi, Wakayama, and Ehime Sanitary Products Company; R&D Laboratories: Tochigi, Tokyo, and Wakayama

HP Domestic offices  
[http://www.kao.co.jp/en/company/group/operations\\_in\\_japan.html](http://www.kao.co.jp/en/company/group/operations_in_japan.html)

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# Through *Yoki-Monozukuri*, we are pursuing CSR activities that share joy with Kao's stakeholders.

## Striving to be a Company that all of our Stakeholders can Trust in and Support

The Kao Group pursues its business activities with the aim of contributing to the satisfaction and enrichment of the lives of people through *Yoki-Monozukuri*. Within that context, the significance of CSR activities lies in reviewing and evaluating our business activities from the perspectives of our various stakeholders and then improving the approaches and systems we use in our business activities.

To continue expanding and developing our business activities, we must, as a member of society, strive to gain the trust of all stakeholders by managing our business in a sound manner. CSR activities are said to be the essence of management and it is from this perspective that I think of them and the economic activities of companies as being the two pillars that support a company.

## Business Activities based on our Corporate Philosophy, "The Kao Way"

Since 2004, when we reviewed our corporate philosophy and restructured it as The Kao Way, I have been encouraging group employees throughout the world to put The Kao Way into practice. The vision of The Kao Way states: "We aim to be a global group of companies that is closest to the consumer/customer in each market, earning the respect and trust of all stakeholders and contributing to the sustainable development of society." This expresses our desire to be closer to consumers/customers than any other company, have a clear understanding of their needs, and be the company they trust most.

Toward that end, we made significant changes to our organization in fiscal year 2006. Specifically, to adjust to various changes in our business environment and develop unsurpassed understanding of consumers/customers, we restructured our business, which had been organized according to product categories, into four consumer-oriented units corresponding to daily living scenarios. We revised the whole concept of our business activities, with the aim of creating systems capable of providing more benefits to consumers/customers.

## Compliance is the Foundation of CSR Activities

To pursue business activities based on The Kao Way, the Kao Group has established Kao's Business Conduct Guidelines as the cornerstone of the activities of individual group employees. We are not satisfied with simply formulating such guidelines. At the Kao Group, members of management take the initiative in consulting our conduct guidelines and pursuing business activities when they are uncertain of how to proceed. We are proactively creating systems to reinforce our conduct guidelines throughout the entire group, including overseas affiliates. We are not only fulfilling our responsibilities as a participant in the Global Compact, which Kao signed in 2005, but are also working to deepen understanding and acceptance of its principles throughout our company.

## CSR Activities for Global Business

In fiscal year 2006, we held six CSR Committees and thoroughly discussed the status of Kao's CSR activities and problems requiring attention. A couple of the new initiatives that resulted are discussed below.

CSR procurement, a prime example of our CSR activities, got under way in January 2007, after the completion of several preparatory steps. CSR procurement takes ongoing green procurement a step further. It considers not only quality and environmental concerns but also human rights, occupational safety, and other corporate social responsibilities and we held explanatory meetings for suppliers and embarked on investigative and other activities to build a supply chain to meet those challenges. Additionally, in April 2007, we joined the Roundtable on Sustainable Palm Oil (RSPO), an international NGO, to discuss the establishment of the sustainable procurement of palm oil, a primary ingredient of our products.

On the environmental front, achieving zero emissions at all domestic plants was a major achievement. In addition, though we operate our proprietary Comprehensive Management System for Chemical Substances to oversee chemical safety and security, we began in 2006 to create a database covering not only domestic laws, regulations, quality-related matters, and labor safety concerns but

also those of other countries. We have now brought this database online as a key system supporting *Yoki-Monozukuri* conscious of the environment, safety and quality concerns from the product research stage all the way through production and distribution.

## Sharing the Joy of Work together with Employees through CSR Activities

For the Kao Group to continue to grow, it is necessary to create working environments that allow a broad spectrum of people throughout the world to work with a sense of security and permit individuals to fully exercise their capabilities. One aspect of this is creating systems that promote healthy work-life balances and facilitate the raising of children.

I believe that a critical responsibility of management in creating such conditions is to deepen understanding and awareness of CSR activities throughout the Kao Group and create systems that promote job satisfaction and personal development for employees throughout the worldwide Kao Group. Therefore, in 2007, we will begin conducting the “FIND” employee opinion survey among group employees throughout the world. Until then, we had performed this survey biannually mainly in Japan. Expanding the survey to cover the entire Kao Group made it possible for us to garner employee opinions from a global perspective and use them to improve our operations.

Since my appointment as president, I have encouraged employees to perform their jobs with enthusiasm and the goal of being a company that we and our customers can share joy about. From a CSR perspective, it could be said that the CSR activities envisioned by the Kao Group are ones that create common understanding with all Kao stakeholders through *Yoki-Monozukuri*.

This Report covers all aspects of the Kao Group's CSR activities, but there are still many initiatives that must be pursued further and issues to address. Looking ahead, the Kao Group will steadily advance its CSR activities and help to build a sustainable society through activities aimed at promoting communication with as many stakeholders as possible.

July 2007

Kao Corporation  
President and CEO  
CSR Committee Chairperson

**Motoki Ozaki**

*Motoki Ozaki*





# Promoting Cleanliness, Beauty and Health for Every Day

## Profile

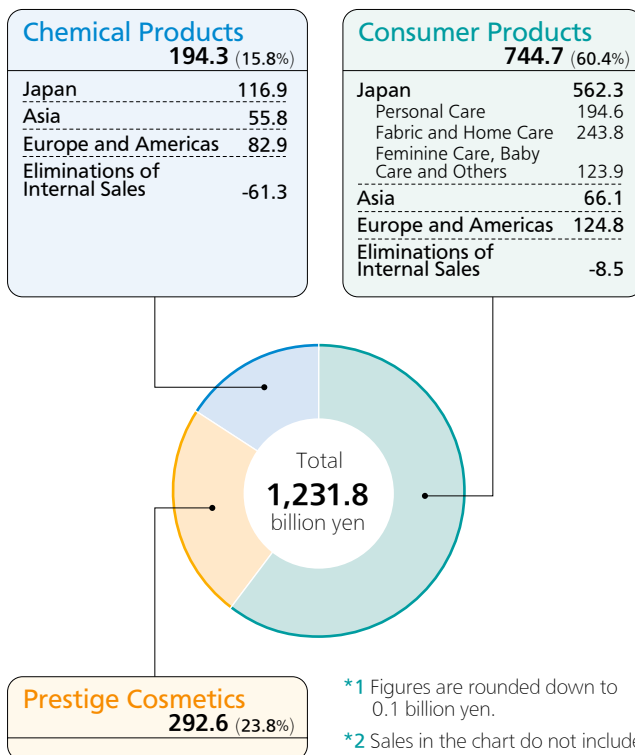
Since its foundation in 1887, Kao has always taken the consumer/customer's perspective and aimed to contribute to society through *Yoki-Monozukuri*. The product group that began on October 17, 1890 with the introduction of *Kao Soap*, the first premium soap to be manufactured in Japan, has now grown to encompass detergents, shampoo, sanitary napkins, and other daily essentials; cosmetics helping women to look their best; and, in recent years, food products promoting health on a daily basis. In addition to these products, which play fundamental roles in promoting cleanliness, beauty, and health, Kao, as a chemical manufacturer, also provides chemical products that are not only superior in function and performance but also environmentally conscious. The Kao group across the globe produces and markets products adapted to local life and industry. We support clean, beautiful, and healthy daily life in locations throughout the world.

## Company Outline (As of March 31, 2007)

Company Name	Kao Corporation
Representative	Motoki Ozaki, President and CEO
Address	14-10, Nihonbashi Kayabacho 1-chome Chuo-ku, Tokyo 103-8210 Japan
Founded	June 19, 1887
Incorporated	May 21, 1940
Capital	85.4 billion yen
Employees consolidated	5,642 (Number of employees in Kao Group companies: 32,175)

## Breakdown of Consolidated Sales (Fiscal 2006)

(Unit: billion yen)

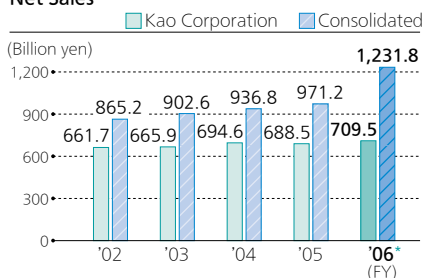


\*1 Figures are rounded down to 0.1 billion yen.

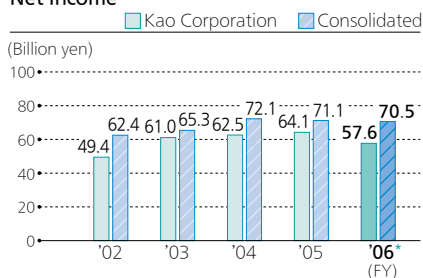
\*2 Sales in the chart do not include Kao Group internal sales.

## Key Management Indicators (\*Inclusion of information on Kanebo Cosmetics in Kao's consolidated results began in fiscal year 2006.)

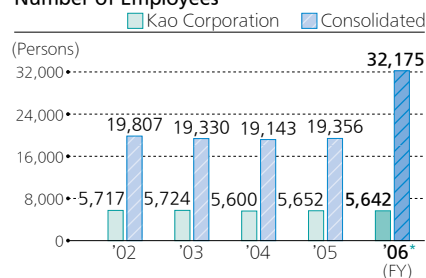
### Net Sales



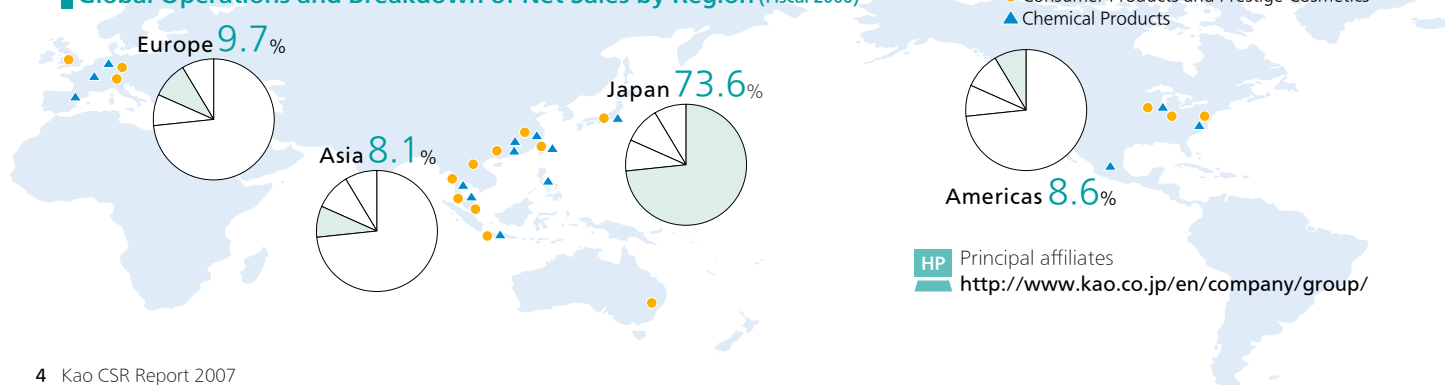
### Net Income



### Number of Employees



## Global Operations and Breakdown of Net Sales by Region (Fiscal 2006)



## Four Business Units

On April 1, 2007, the Kao Group began to plan, develop, produce, and market high-quality products that make daily life cleaner, more beautiful, and healthier through the four business units described below.

### Beauty Care

Responding in total to the desire to be beautiful

Skincare cosmetics, foundation, makeup cosmetics, facial care products, body care products, hair care products, hair styling products, and hair coloring products



### Human Health Care

To make every day more comfortable and healthier — Daily health care for the mind and body

Cooking oil, dressings, mayonnaise-type sauces, beverages, bath additives, oral care products, sanitary napkins, disposable diapers, nursing care products, and hygiene care products



### Fabric and Home Care

Promoting comfort and fun in daily life

Laundry detergents, fabric softeners, kitchen cleaners, and household cleaners



### Chemicals

Unique Kao products and services contributing to tomorrow's industry in amazing ways

Oleochemical products (fatty alcohols and their derivatives etc.), performance chemical products (surfactants, etc.), specialty chemical products (information materials, fragrances etc.)



# Yoki-Monozukuri in All Corporate Activities

## Kao's Corporate Philosophy and CSR

In October 2004, Kao formulated The Kao Way as an expression of Kao's unique corporate culture and spirit of enterprise; The Kao Way is a statement of the corporate philosophy underlying our corporate activities. Kao's CSR activities are not simply daily implementations of the *Yoki-Monozukuri* spirit expressed in the values of the Kao Way. Our CSR activities are put into practice on an ongoing basis through all of our corporate activities and in

our relationships with all our stakeholders. Through our CSR activities, we pursue fairness in the economic aspects of our business activities, doggedly strive to solve environmental problems, and undertake activities to meet our various responsibilities to society. Moving forward, Kao will continue to contribute to the sound development of global society through *Yoki-Monozukuri*.

## The Kao Way

### Mission

Our mission is "to strive for the wholehearted satisfaction and enrichment of the lives of people globally" through the Company's core domains of cleanliness, beauty, health, and chemicals. Fully committed to this mission, all members of the Kao Group work together with passion to provide products and brands of excellent value created from the consumer/customer's perspective. In so doing, we "share joy with the consumer/customer."

### Vision

We aim to be "a global group of companies that is closest to the consumer/customer in each market," earning the respect and trust of all stakeholders and contributing to the sustainable development of society.

### Values

**Yoki-Monozukuri** Fusing Needs & Seeds  
Uniting Abilities  
Yoki-Monozukuri Cycle

**Innovation** Continuous Improvement & Innovation  
Never Being Satisfied with the Status Quo  
Difficulties Are Opportunities

**Integrity** Respect, Fairness, Sincerity & Diligence  
Behaving Lawfully & Ethically  
Responsible Corporate Citizen

### Principles

**Consumer Driven** The Consumer Is Our First Priority  
Be Close to the Consumer  
Communicate with the Consumer

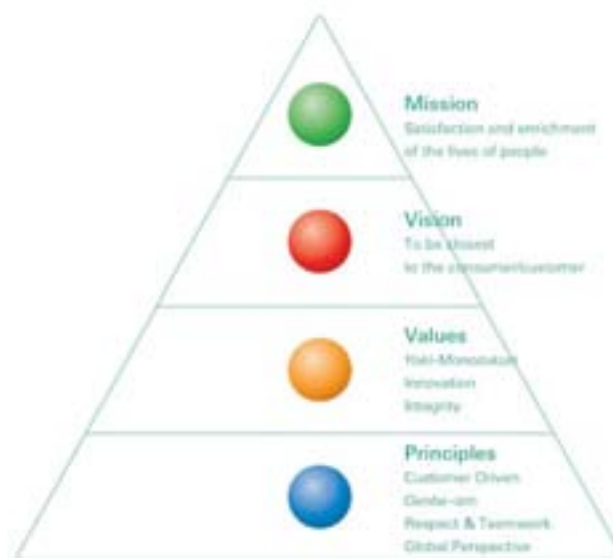
**Genba-ism\*** Understand the Consumer *Genba*  
Unification through Knowing *Genba*  
Inspiration from *Genba*

**Respect & Teamwork** Respect Diversity  
Maximize Individual Capabilities & Performance  
Enhance Active Communication  
Cooperate with Business Partners

**Global Perspective** Understand Local Needs  
Develop Suitable Local Business Operations  
Be Open to New Ideas  
Global Optimization

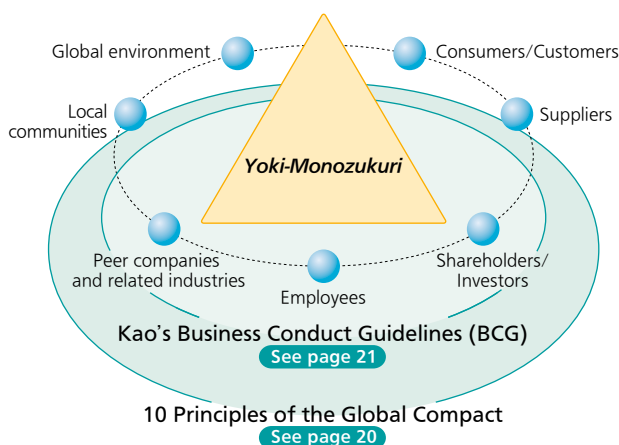
#### \* Genba-ism

"Genba" literally means "actual spot". As Kao, this term refers to the importance of observing things in their actual location and environment so that we can understand our business and optimize performance.



HP Entire text of The Kao Way  
<http://www.kao.co.jp/en/company/kaoway/>

## CSR Activities through Yoki-Monozukuri





## Kao's Stakeholders

- Key Communication Opportunities
- Key Communication Tools

### Consumers/Customers

Kao identifies consumer/customer needs and provides them with products and brands that give them satisfaction and joy. Kao develops products that are not only functionally superior and emotionally appealing, but also user-friendly – usable by everyone, regardless of age and ability. Also, we endeavor to develop safe products with less environmental impact so that people can use them with peace of mind. Kao proactively provides accurate information about its products to consumers/customers.

#### Chemical and Professional Product Customers

- Meetings held to exchange views with dealers
- Chemical and C&S Exhibits
- Extranet providing links to dealers
- Kao Chemical Forum
- Web site (Chemical and professional products)

#### Consumer Products Retailers

- Product study meetings
- Discussions with leading retailers
- Exhibitions

#### Consumers

- Focus groups
- Home visits to consumer monitors
- Consumer consultation service
- *Relief-fureai* call service
- Counseling at cosmetics retail locations
- Kao Corporate Profile
- Web site
- Product news releases
- Kao Consumer Communication Activity Report

### Employees

Kao respects the human rights, individuality, and diversity of each employee, and maintains a safe and comfortable work environment. We evaluate each employee's performance fairly and helps them develop their capabilities and personality through their work by providing challenging opportunities.

- Employee meetings with top management
- Health and Safety Committee
- Compliance Reporting Hotline
- Mental Health Counseling
- FIND (Employee opinion survey)
- *Te-ni-te* (Internal well-being journal)
- *Kao Family* (Internal newsletter)
- Kao News Quarterly (English-language internal newsletter)
- Work and Life Balance Guidebook
- Kao's Business Conduct Guidelines

### Suppliers

Kao ensures fair and transparent transactions. Together with suppliers, Kao tries to enhance supply chain management and works on various social issues, including protection of the environment and human rights.

- Meetings held to exchange views with suppliers
- Quality improvement meetings, environmental surveys
- CSR procurement surveys
- Supplier satisfaction surveys
- Guidelines for Procurement of Raw Materials
- CSR Procurement Guidelines

### Shareholders/Investors

Kao earns the support and trust of its shareholders by raising corporate value through profitable growth. We achieve this by further building existing businesses, nurturing new ones and expanding overseas. Moreover, we strengthen and enhance corporate governance while strictly managing information and assets.

- General shareholders meetings
- Financial results briefings
- Investor visits
- Business Report
- Business Results
- Annual Report
- Web site (Investor information)

### Local communities

Besides complying with laws and regulations and meeting the tax obligations, Kao is actively promoting dialogue with local communities where it operates businesses, as well as giving full consideration to environmental conservation and human rights to contribute to community development as a member of the local community.

- Meetings with local residents, joint events
- Factory tours
- Corporate citizenship activities and meetings with NPOs
- Environmental/safety site reports
- Web site (Social/cultural activities)

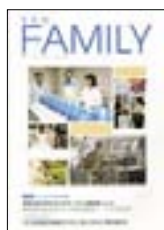
### Global environment

Kao promotes anti-global warming measures and is contributing to the creation of a recycle-based society by implementing 3R (Reduce, Reuse, Recycle) initiatives. In particular, the company focuses on proper management of chemicals – from raw materials through to their disposal.

- Peer companies and related industries
- Government/industry committees
- Consumer consultation service
- Environmental communication
- CSR Report
- Web site (Environmental initiatives)
- Daily Living Information on Environment and Safety
- Daily Life and the Environment

### Peer companies and related industries

- Joint research with peer companies, etc.
- Industry activities
- Media (Newspaper, magazine, TV) coverage
- Meetings with media reporters
- Government-sponsored committees
- Relevant academic association meetings, joint research with research institutes
- Recruiting activities, surveys
- News releases
- Web site
- Kao Health Care Report



Kao Family  
(Internal newsletter)



Annual Report



Consumer consultation



Meeting with suppliers



Environment surveys  
(Teacher fellowship)

# Kao' Health Care Food Business — Responding to the voices of people seeking health for every day

— From *Econa Cooking Oil* to *Healthya Green Tea*, putting *Yoki-Monozukuri* into practice

As lifestyle-related diseases caused by obesity cast an ominous shadow over the health of Japanese, Kao has combined consumer needs identified through meticulous market research and knowledge, as well as basic technology it amassed in the area of fats and oil science through cooking oil development, to create *Econa Cooking Oil* and *Healthya Green Tea*, two of the leading products in our health care food business. Within this development process, Kao employees pursued *Yoki-Monozukuri* through repeated communication with various stakeholders both inside and outside the company.

## INFORMATION

### Lifestyle-related and Food for Specified Health Use

According to research by the national government, the westernization of the Japanese diet is causing people to take more fat, and that, combined with a lack of exercise, has resulted in a growing number of Japanese who are obese. The fiscal year 2003 National Health and Nutrition Survey found that one out of three men in their 30s to 60s were obese. Being obese is a risk factor for the development of lifestyle-related diseases and the danger of symptoms referred to as "metabolic syndrome" has recently come to light. In metabolic syndrome, people develop multiple lifestyle-related diseases, like hyperlipidemia, high blood pressure, and diabetes, due to an excessive accumulation of visceral fat. To promote healthier lifestyles, the national government, since implementing the Food for Specified Health Use (FOSHU) system in 1991, has announced a series of new measures.

#### Key Lifestyle-related Disease Prevention Measures

- 1978:** First-phase Measures for National Health Promotion
- 1988:** Second-phase Measures for National Health Promotion
- 1991:** Implementation of the "Food for Specified Health Use" system
- 2000:** Creation of "Healthy Japan 21"
- Announcement of stronger policies for increasing awareness of the importance of preventing metabolic syndrome, exercising regularly, and improving eating habits.
- 2003:** Implementation of the "Health Promotion Law"
- Creation of systems at the local government level for supporting individual health efforts
- 2005, April:** Creation of standards for diagnosing metabolic syndrome

#### Food for Specified Health Use (FOSHU)

"Food for Specified Health Use" (FOSHU) is a food item with an ingredient, or ingredients, that have positive effects on the body's physiological or other functions. These food items can bear labels informing consumers that they can expect a specified health benefit, like improvement of gastrointestinal function, from taking them. Before a food item can carry such health benefit information on its label, however, it must undergo an examination of the scientific bases for its effectiveness and safety regarding individual physiological and specified health functions, and be approved by the Minister of Health, Labour and Welfare (Article 26 of the Health Promotion Law). Products that are approved carry a special mark signifying their approval.

## Phase 1 The Econa Epoch

### *Econa* a great success in the use of original technology to respond to society's demands for measures to fight lifestyle-related diseases

In February 1999, Kao announced that it had obtained Food for Specified Health Use (FOSHU) (See the column at left) approval for *Econa Cooking Oil*, the first cooking oil in Japan to bear the words "Less likely to become body fat" on its package. The characteristics of *Econa*, which was advertised as a cooking oil that promotes better health and can be eaten easily on a daily basis, made it popular not only among consumers worried about lifestyle-related diseases caused by excessive weight but also among doctors, dieticians, and other specialists, who welcomed it with great interest. With sales during the first two weeks twice as high as initial plans, *Econa* became a hit product.

Development of *Econa* began in the 1980s, when a researcher took an interest in a byproduct obtained while working on another substance. What piqued his interest was the digestive function of diacylglycerol, which is found in small quantities in natural fats or oil. After that initial spark, Kao researchers spent the next 15 years analyzing and evaluating diacylglycerol's lipid metabolism mechanism from all angles. Ultimately, the interest of a single researcher resulted in Kao's staff making discoveries and developing knowledge in the areas of nutrition, metabolism, and anti-obesity research, and finally to the creation of the epoch-making product that is *Econa*.





## Phase 2 Making a Business Out of Health Care Food

### The beginning of the Health Care Food Project focusing on a third function of food

Encouraged by the success of *Econa* and society's growing interest in lifestyle-related diseases, Kao launched its Health Care Food Project in 2000. The purpose of this project was to identify and take advantage of the third function of food — that being the regulation of body functions, or keeping the body in healthy condition — and develop of food products that could be eaten easily on a daily basis. (The first function of food is nutrition, or the provision of nutrients necessary for life. The second function is gustatory satisfaction.) Taking that as its cue, the business division embarked on painstaking market research seeking to identify products that could be consumed daily or habitually, are preferred by consumers concerned about their weight, and could gain FOSHU authorization.

Meanwhile, Research & Development began screening over 100 types of food ingredients based on the analytical and evaluation technologies developed in the process of shedding light on diacylglycerol's mechanisms. After much trial and error, they discovered that tea catechin, a type of polyphenol found in tea leaves, has the property of suppressing the accumulation of visceral fat. What came out of the fusion of this knowledge with market research results was *Healthya Green Tea*.

*Healthya Green Tea* is an exemplary Kao product resulting from the combination of consumer needs data gained from thorough market research and technical seeds developed by our Research & Development Division.

## Phase 3 Commercialization of *Healthya Green Tea*

### Matrix management facilitates communication among R&D experts from both inside and outside the company and improves functionality, quality, and development speed

At Kao, once a product concept has been determined, significant amounts of dialogue among technical experts inside and outside the company come into play to achieve improved product functionality and quality, and greater development speed, in commercialization. Supporting that effort is matrix management, which drives commercialization forward as it cross-functionally utilizes results from both basic technology and product development research.

In the development of *Healthya Green Tea*, our Health Care Food Research Laboratories took the lead in establishing "health functionality" and "taste and flavor" development axes and overseeing product development. On the health functionality axis, the Biological Science Research Laboratories examined mechanisms for activating lipid metabolism and fighting obesity. On the taste and flavor axis, flavorists at the

## Putting The Kao Way into Practice: Innovation

### Listening to consumers and retailing customers, and rising to the challenge of planning products that are full of originality

Kazuhiro Tashiro (Food & Beverage Business Group, Development Leader)



Wanting to create products that can contribute to the health of as many people as possible, we focused our attention on beverages, which are a part of daily life. The beverage market is one in which competition is fierce and large numbers of new products appear and soon disappear, but we took up the challenge of beverage development based on the belief that a truly useful product could gain long-term consumer support. We worked to perfect the product right up to the point of its launch by carrying out numerous studies and holding countless discussions. In our sales strategy, we considered the need to make the product easy for business people to purchase. We initiated sales at some convenience stores, and expanded our sales channels once the prospect of sufficient volume production to support stable supplies became clear. The work of product development consists of cooperating with the Research & Development Division in pursuit of *Yoki-Monozukuri* that is truly useful to consumers, and realizing Kao's product strategy. We want to continue carefully listening to consumers and developing products that are full of originality and represent the best that Kao has to offer.

## Putting The Kao Way into Practice: *Yoki-Monozukuri*

### Working to build a quality management system

Satoshi Imanari (Quality Management Center, Food Quality Management Section)



Food products require strict quality assurance. At Kao, therefore, we created our Food Quality Management Office to specialize in assuring the quality of food products. This office engages in a high degree of information sharing with related divisions, holds regular meetings not only inside the company but also with raw materials suppliers and manufacturing subcontractors, occasionally invites suppliers as speakers for study meetings, and undertakes other initiatives in an effort to build a quality management system that covers the entire supply chain. In undertaking these activities, the office focuses, for example, on providing explanations, including scientific data, as to why a manufacturing subcontractor is being asked to fulfill disinfecting or other management conditions. We believe that, as a result, we can not only gain simple compliance with rules but also foster more sophisticated quality awareness. For Kao, the area of food products is one that carries high priority for its potential development into a principal business. My aim is to continue supporting consumers' peace of mind regarding Kao food products by furthering the work of building organizations and management systems guaranteeing high quality.



Taste and flavor analysis



Kao' Health Care Food Business — Responding to the voices of people seeking health for every day

— From *Econa Cooking Oil* to *Healthya Green Tea*, putting *Yoki-Monozukuri* into practice

### INFORMATION

### Health Care Research Center

The Kao Health Care Research Center was completed in February 2004 as Kao's integrated research center for health care products. In its health care product development and research area, the center includes facilities allowing the integrated pursuit of clinical research on nutrient metabolism, taste and flavor research, and research on production processes. The fragrance development area performs product fragrance development and evaluation from the consumer's perspective, analyzes smells, and does research on fragrance creation.



#### Introduction of Cutting-Edge Facilities

A Dual Energy X-ray Absorptiometer (DEXA) can easily take measurements of total body fat, muscle, and bone density, is less burdensome for patients than traditional MRI technology, and produces highly accurate results. In anti-obesity research, a DEXA is very useful for purposes like measuring changes in the total body fat of research subjects. The Human Metabolic Chamber is a living space that provides an environment that closely duplicates eating, exercise, work, sleep, and other aspects of daily life and is capable of measuring the energy consumption of research subjects over a long period of time. The Human Metabolic Chamber installed by Kao is the third such facility in Japan; the other two are at the National Institute of Health and Nutrition and the University of Tsukuba.



#### Kao Presented with the Nikkei "Monozukuri" Award

The Kao Health Care Research Center was presented with the 2006 Nikkei "Monozukuri" Award (sponsored by Nikkei Inc.). The purpose of this prize is to recognize outstanding manufacturing and research facilities and the programs and systems they use. The Kao Health Care Research Center, in particular, was praised for its concentration of leading-edge research functions that have played key roles in the development of *Econa*, *Healthya*, and other healthcare products.

### From a Stakeholder

#### Expectations of returns to society from Kao's research results

Japan is seeing unprecedented aging in its population and it is said that we are now in the midst of a "health boom." In reality, however, we walk less, have decreased our intake of vegetables and fish, and, as a result, metabolic syndrome is now a problem affecting approximately half of adult men and 20% of middle-aged and elderly women.

Metabolic syndrome can be avoided by taking care to eat and exercise properly, but the reality is that even if we understand the health benefits of a good diet and exercise, few are able to act on that knowledge on a continuous basis. I, therefore, have great expectations for the development of new food products that are easy to prepare and tasty, and that painlessly contribute to good health. If, as a result, it is possible to lighten the mental burden of feeling we cannot eat when we really want to, it should also become easier to improve our diet.



Kagawa Nutrition University Vice President Professor  
Yasuo Kagawa

Perfumery Development Research Laboratories spent about a year visiting tea farms throughout the country. Meticulous research was performed on the different flavors produced by various types of tea leaves and tea preparation methods, and the cooperation of the Analytical Science Research Laboratory was enlisted to analyze tastes at a molecular level. Additionally, these research results were verified by a third-party clinical testing laboratory to obtain the data necessary to apply for FOSHU approval. At the same time, our Production & Engineering Division was developing production technology for suppressing the bitterness of concentrated tea catechin (the result of Kao research) and reproducing the full taste and flavor of a freshly prepared tea.

*Healthya Green Tea*, the culmination of Kao's leading-edge research in a variety of fields, was approved by the Ministry of Health, Labour and Welfare as a Food for Specified Health Use in March 2003.

### Phase 4 Information Dissemination and Awareness Activities

#### In meeting our social responsibilities as a manufacturer, we are actively disseminating information

In May 2003, Kao introduced *Healthya Green Tea*, which has been approved to carry a FOSHU seal on its label. The name, "*Healthya*," is derived from the words "healthy assist" and expresses the development concept of supporting health on a daily basis through scientifically grounded functional foods.

Disseminating accurate information with the goal of achieving widespread understanding of product functions among consumers is in the interest of promoting consumer safety and health, and is a basic social responsibility of a manufacturer. In particular, it is important for consumers to have a correct understanding of the functions and uses of FOSHU-approved products. Kao's education activities help to establish faith in the FOSHU system and boost awareness of the importance of maintaining good health.

Kao issues the Kao Health Care Report, which includes information from sources like research reports on the roles of diacylglycerol and tea catechin in lipid metabolism, and news about the latest scientific research results on the prevention of obesity and lifestyle-related diseases. We also hold the Kao Health Care Forum, to which we invite members of the media, and encourage doctors and dieticians to participate in seminars and discussions.



Website: *Healthya Green Tea*



Website: Nutrient Metabolism R&D



Healthya Water in a retail store

## Phase 5 Ongoing Technological Innovation

### Putting The Kao Way into practice *Healthya Water* was developed to boost the conversion of fat into energy

At Kao, which offers many products that are integral to daily life, we are constantly developing and improving products based on the *Yoki-Monozukuri* and Innovation written in The Kao Way. After developing *Healthya Green Tea*, our technical staff carried on with its multidimensional research on tea catechin, while our marketing staff formulated and tested multiple hypotheses in pursuit of additional possibilities in the beverage market.

*Healthya Water*, which was introduced in May 2006, was one result of this work. Aiming to go a step beyond appealing to people concerned about body fat, the aim of *Healthya Green Tea*, our development staff established the goal of gaining approval for a message that would clearly express the effect of tea catechin, and went in search of scientific data showing that ongoing consumption of tea catechin promotes the burning of body fat. After much work at both internal and external research facilities, we launched the first sports drink with FOSHU approval of a message telling consumers it boosts the conversion of fat into energy. As an added benefit, *Healthya Water* incorporates the use of technology that greatly reduces the bitterness of tea catechin and allows us to recommend this product particularly to those who dislike a bitter taste.

Kao, which has positioned its *Healthya* products business as one of its principal operations, will work to further increase the value of its *Econa* and *Healthya* brands, continue with R&D and marketing initiatives, and, thereby, help people to enjoy diets that are healthier and more enriching.

## Putting The Kao Way into Practice: Consumer Driven

*I want to increase trust in, and expectations of, Kao through information provision from the consumer's perspective*

Kahoko Kanatani  
(Consumer Communication Center)



The mission of the Consumer Communication Center, where I work, is to disseminate appropriate product information. We work to provide as many people as possible with accurate information on the functions and safety that can be expected of *Healthya Green Tea* and other FOSHU-approved health care food. We pay particular attention to providing information to dietitians, who are food experts at the local area. Dietitians promote better health through participation in citizens' health seminars and other such events, through the dietary guidance they provide at companies and hospitals, and in the work they do in many other aspects of daily life. We want dietitians to be a channel for providing correct product information to large numbers of consumers. Additionally, because of the importance of the link between *Healthya Water* and exercise, we are building a new network for communication with health fitness programmers.

### From a Stakeholder

#### Expectations and demands regarding Kao's health care products

Presently, there is much interest in the health of the Japanese population, and a wide variety of information is being provided via the media. However, even if correct, detailed information is being provided, I have serious doubts as to whether it is being properly understood. A large variety of health care foods are available in the market, but I feel that very few people use these health care foods based on a solid understanding of what and how much they should take. I believe that it is necessary for government and relevant companies to cooperate and seriously examine what should be done, so that people can use these products based on sound understanding.



Japan Dietetic Association  
Executive Director  
Shinji Kawana

## INFORMATION

### Information Dissemination and Awareness Activities

In its health care food business, Kao disseminates information gleaned from scientific data on the mechanisms and functions of food ingredients, and information useful for improving daily life. The purposes of these activities are to provide information that allows consumers to use our products with peace of mind and to help improve human health. In pursuing these activities, we provide information to consumers and the media, and are reinforcing our dissemination of nutrition and metabolism and other expert-level information to doctors, dietitians, and others with social responsibilities in fields like diet improvement and obesity prevention.

#### ● Holding of Seminars and Symposiums

Kao, through its Research & Development Division, sponsors and supports seminars and symposiums for doctors, registered dietitians, and other experts in nutrition and metabolism.



#### ● Support for the Retailing and Food Industries, and for Governmental Organizations

Kao provides instructors for training sessions and seminars held by the food industry, local governmental organizations, and others. We also cosponsor and support these activities in other ways. Additionally, Kao Healthy Diet Advisors disseminate information within each community.

#### ● Support for the Activities of the Japan Dietetic Association

Kao provides instructors for training sessions and seminars held by the Japan Dietetic Association, which plays a leading role in improving the Japanese diet. Dietitians, for their part, assist us by providing nutritional advice in retail settings.



#### ● Establishing and Managing the Kao Research Council for the Study of Health Care Science

Kao Research Council for the Study of Health Care Science is useful for furthering research on topics like lipid nutrition and lifestyle-related disease prevention. While assisting with research in these areas, this council also issues the Kao Health Care Report, which carries information on research results and the latest health-related news.



# Aiming to establish a sustainable production system responding to growing world demand

— Initiatives by the overseas affiliate Pilipinas Kao

Kao's fatty alcohols, which are made from renewable vegetable oil, have seen a rapid increase in demand due to worldwide economic growth and heightened interest in environmental problems.

In response, our local affiliate in the Philippines, Pilipinas Kao, completed construction of a new facility in 2006.

This facility is intended to provide a stable supply of products to the world market. It promotes low-environmental-burden, high-quality product manufacturing, as well as safe and comfortable working conditions.

Furthermore, through proactive hiring of local people, communication with local communities, and

product exports, it is pursuing *Yoki-Monozukuri* together with the Philippine economy and the local community.

The new Pilipinas Kao production facility aims to achieve sustainable growth.

## Angle 1 Stable Supplies to the World Market

### Construction of a new plant to stably supply the world market with fatty alcohol products made from renewable resources

Fatty alcohols are the main products of Kao's oleochemical business (See page 13). Kao's fatty alcohols, which are made from coconut and palm oil, are widely used by industry to produce laundry detergents, shampoos, and other household products, and as additives for various plastic products. Demand for fatty alcohols has grown year after year, along with the global economy, and Kao has expanded its production capacity in a step-by-step manner. Furthermore, as the rapid growth of the BRICs and other emerging economies has accelerated demand growth for the raw materials including petroleum and driven the prices of petrochemical alcohols up, and amid factors like heightened worldwide interest in global environmental problems and a recycling-based society, interest has focused on products made with vegetable oil, which is a renewable resource.

Within that context, our Philippine affiliate, Pilipinas Kao, Inc. (PKI), completed construction of a new facility in December 2006, expanding its annual production capacity by 2.5 times, to 100,000 tons. That increased the Kao Group's overall annual production capacity to approximately 300,000 tons, creating the ability to stably supply the world market and making Kao one of the world's leading providers of fatty alcohols.

## Angle 2 Contributions to Local Economies and Communities

### Contributing to the improvement of daily life and culture in local communities and the sound development of industrial communities

Within the Kao Group's chemical business, which has global operations, PKI, established in 1977, has a pioneering presence. In its operations, PKI was quick to implement Kao's globalization concept of "stably supplying world markets, while contributing to daily life and culture in local communities and the sound development of industrial communities." To illustrate, before the decision to establish PKI was made, the Philippines, as an industrialization initiative, was attempting to develop a chemical industry that would use coconut-based raw materials, and was actively recruiting participants. Kao then decided to establish PKI to stably supply products and contribute to Philippine communities. When we selected a local partner company, we examined candidates' ethics and management performance, and whether they would proactively hire people living in the communities adjacent to PKI. Additionally, we have promoted activities to strengthen connections with local communities (See page 14).

Presently, about half of the approximate 100 people employed by PKI are from the local community called, "Jasaan

#### Overview of Pilipinas Kao

Location:	Philippines
Business Activities:	Manufacturing and sales of chemical products made from coconut oil
Employees:	140
Capital:	433.8 million pesos
Ownership Percentage:	Kao 100%



City." Furthermore, PKI, a PEZA<sup>\*</sup>-registered company, is now using approximately 10% of the Philippines coconut production to produce high-value-added fatty alcohols. Exporting approximately 90% of its production, PKI is contributing to the development of Philippine economy.

<sup>\*</sup> Philippine Economic Zone Authority. PEZA provides tax and other preferential treatment for companies that, in principle, export at least 70% of their production.

### Angle 3 Measures to Address Global Environmental Problems

#### Building and operating environmental management systems in accordance with Kao's environmental management standards

Global environmental problems, it goes without saying, present business continuation concerns for Kao's chemical business, which uses vegetable oil as its primary raw material. However, they are also problems that cannot be ignored by the Kao Group, which seeks the creation of a sustainable society. PKI, of course, complies with the environmental laws and regulations of the Philippines, but also uses Kao's environmental management system. That system complies with Japanese laws and environmental standards, which, depending on the regulatory item, may be stricter than the comparable Philippine counterpart. Operation of the system is being pursued as management uses objectives like acquiring ISO14001 certification to raise awareness of the importance of participation among employees. In its production activities, PKI has converted to low-sulfur fuel and taken other measures to protect the local area's beautiful natural environment and air.

### Putting The Kao Way into Practice: Global Perspective

#### Trust of local communities supported project accomplishment

Shuhei Arikita (PKI Plant Manager)



Regarding plant construction and maintenance work, we endeavored to contribute to the local community by, for example, signing an employment memorandum with the local government. Through other such efforts over the years, PKI has won the goodwill of the local community. The resulting, positive word-of-mouth messages communicated by numerous community members talking about relatives or friends working for PKI, contributions made by PKI, etc. have made it easier to secure construction workers and hire employees, negotiate with government offices, hold briefings for local residents, and accomplish other aspects of our business.

### Putting The Kao Way into Practice: Innovation

#### Embarked on development of a high-quality, low-environmental-burden catalytic process

Takanobu Katayama  
(Processing Development Research Laboratories)



For Kao, which is a leading provider of fatty alcohol in the global market, increasing the capacity to produce cost-effective products of superior quality could be called a social mission. At the same time, it is essential to establish a production process with a lower environmental burden. In fulfilling the missions mentioned above, I am proud that the technical staff of which I am a member were able to provide new value by carrying out round after round of trial and error utilizing the substance and reaction data, as well as analytical expertise developed by earlier generations rising to meet the challenges of their day. Using the advanced catalytic and process engineering technologies that have been handed down to us, we will continue to rise to the challenge of *Yoki-Monozukuri*.

## INFORMATION Kao' Chemical Business

The chemical arm of the Kao Group, which is comprised of three principal businesses, generates annual sales in excess of 220 billion yen<sup>\*</sup>.

<sup>\*</sup> Includes internal sales of raw materials for cosumer products.

<b>Oleochemical Business</b>	Kao's oleochemical business, with catalytic and processing technology at its core, supplies the world market primarily with fatty alcohols and their derivative products such as tertiary amines, which are mainly products used as raw materials for dishwashing detergent and hair conditioner.
<b>Performance Chemicals Business</b>	Kao's performance chemicals business provides unique performance chemical products relying primarily on surfactant technologies in emulsification, dispersion, and surface modification to respond to the needs of customers in the construction, pulp and paper, plastic, and food industries etc.
<b>Specialty Chemical Business</b>	Kao's specialty business, working with core technologies in polymer molecular design and pigment dispersants, offers information materials, such as toner for copiers and printers, ink and colorants for inkjet printers, polishing agents for hard discs, and fragrances applying organic synthesis technology.

#### Principal Environmentally Conscious Products

##### Powerful Aqueous Cleaner, Cleanthrough Series of Cleaning Products

Coolants and solvents that contain CFC substitutes and are used in the manufacture of electronics are targeted for reduction in the Kyoto Protocol. As an alternative, Kao offers the *Cleanthrough* Series of powerful cleaners, which are water-based but offer the same cleansing performance as solvents.



##### KB Series of Bulk-Increasing Agents

Using its surfactant technology, Kao has commercialized its *KB* Series of bulking promoters, which are used in the process of making paper. Bulking promoters allow manufacturers to make paper that is as thick as other paper, but weighs less. They also make it possible to reduce the use of pulp bleach and bleaching agents for pulp.



##### EG Runner Casting Runners

*EG Runner* developed by Kao Quaker is made with recycled paper, reducing 90% of cutting dust and other waste. Furthermore, energy can be saved in transportation and use, because of its light weight and sufficient durability.



##### Viscotop High-Performance Specialty Thickener

*Viscotop's* higher-order structure formed by of surfactants controls the viscoelasticity of water. This allows cement slurry and mortar to harden in water, without materials segregation, and, thereby, promotes bank-protection and harbor construction without attendant water pollution.



## Feature Report II: Chemical Business and CSR

Aiming to establish a sustainable production system responding to growing world demand

— Initiatives by the overseas affiliate Pilipinas Kao

### Putting The Kao Way into Practice: Respect & Teamwork

**Project accomplished by respecting individuals and emphasizing teamwork by delegating authority to the local staff**

Koji Otsuki (Production and Engineering Division, Chemical SCM Center)



In our project, we delegated authority to a great extent, aiming to secure the safety and boost the morale of employees. With the basic policy of having Japanese staff focus on providing advice, we assigned people, based on their personalities, tendencies, and aptitudes to positions in construction, operational testing, and commercial operation, and appointed those with appropriate capabilities to be leaders at every stage. Because leaders developed strong awareness and a sense of responsibility, local staff came to perform their jobs with a sense of ownership, and the strong feeling of unity as a team emerged in the workplace. That, in turn, encouraged knowledge acquisition, productivity improvements, and safety rule compliance among individual employees, and boosted organizational productivity and learning capacity. Because of their efforts, 2,000 people gathered in this project at its peak, was able to achieve the goals of suffering no accidents and meeting deadlines.

### Voice

**Human Resources and Relations Development Committee (HRRDC), Representative**

As a member of the HRRDC, I am trying to make the company into one where everyone helps each other. The vehicle for doing this is activities aimed at creating a better working environment with systems that my fellow employees can trust and guarantees of fair compensation. At each month's meeting, I think of how to make things go as smoothly as possible, as I hear the opinions of many employees and consider the ideas of management. I feel the difficulty of fulfilling my responsibilities at times when I cannot attend meetings because I am too busy with my main job and when my fellow employees expect too much of me. In the end, however, I am happy when the accomplishments of HRRDC result in the improvement of benefits and policies for the employees.



PKI Production Division  
Dindo Cabello

### Angle 4 Creating Safe and Comfortable Working Environments

**Holding monthly Human Resources and Relations Development Committee Meeting, where employees and management discuss ways to improve working environments**

PKI undertakes various activities aimed at achieving zero work accidents, as provided in the Kao Group's Occupational Safety & Health Management Rules (See page 28). In pursuing these activities, management and employees engaged in ongoing discussions aimed at creating safer, more comfortable work environments. In more specific terms, PKI has, in consonance with the theme of creating a motivating work environment, created its Human Resources and Relations Development Committee (HRRDC) within which representatives of each division and management exchange views on a wide variety of topics, including safety and health, vacation time, and company benefits.

In response to employee opinions and suggestions, the HRRDC now meets more than once a month and, in fiscal year 2006, revised retirement benefits, accident insurance benefits, and other rules under the theme of creating a motivating and safe workplace. It was also decided that PKI will acquire the OHSAS18000 international labor safety management system certification during fiscal year 2007.



Project member meeting

### Principal Community Interaction and Social Contribution Activities Implemented in Fiscal Year 2006

Working from the concept of improving the quality of life of the poor through programs that result in self-reliance, PKI undertakes various community interaction and social contribution programs. These programs are created based on discussions in CSR Councils.

#### Educational Support

##### Launch of a new scholarship system

PKI has created its own scholarship system for Xavier University, in Cagayan de Oro City, and for Mindanao Polytechnic State College, in Jasaan City. This system, which was inaugurated in fiscal year 2006, will provide scholarships to 10 outstanding students who advance to high school in the Luz Banzon and Solana districts.



#### Contributions to Local Communities

##### Use of PKI fire engines to fight fires in local areas

PKI, which is equipped as a modern chemical plant, has fire engines to put out a fire should one occur and regularly carries out training to fight fires. There are no fire engines, however, in Jasaan City, where PKI is located, so when there is a fire in or near the city, PKI sends its fire engines to fight it.







Construction completion ceremony

## Angle 5 Relations with Local Communities

### Holding CSR Councils to work in unison with local residents to solve problems

PKI is located in Jasaan City, which is about 1,400 km south of the capital, Manila. The city is in the northern section of Mindanao island, in a lush natural forest. There are few large companies and daily life for most people is hard. Therefore, in 2005, PKI employees and selected residents\* of the neighboring Luz Banzon and Solana districts came together to establish the Kao-Barangay CSR Council. The purpose of this council is to solve lively-hood, health and sanitation, education, environmental, and other problems facing local people. In regular monthly meetings, residents and PKI employees discuss issues and concerns on their minds, identify specific actions to take, approve plans, and report on the status of ongoing work.

\* Four participants from the Barangay Luz Banzon and 3 from the Barangay Solana. Barangays are the smallest unit of local government in the Philippines.

#### Main Activities Planned and Implemented by the CSR Councils

##### Fiscal Year 2006

- Welding training for local resident volunteers
- Contributions of educational toys for mentally disabled children
- Contributions of educational equipment to local community associations. DVD players, TVs, etc. for teaching preschoolers
- Installation of street lighting

##### Up to Fiscal Year 2005

- Distribution of coconut seedlings
- Dental and medical outreach for local residents
- School repairs
- Employment of local residents for construction of the new PKI plant and facility maintenance

## Voice

### Local Resident Member of the CSR Council

The CSR Council is a valuable place for open communication with PKI employees and management. It allows us — local residents — to understand PKI's mission and vision, values, and environmental policies, and lets PKI deepen its understanding of what we are thinking. Projects discussed and decided on with such mutual understanding work in the interests of both PKI's business and daily life for local residents, and have become a foundation of mutual respect and trust. Looking to the future, I am expecting to further discussions and see PKI continue to emulate the OECD's Code of Conduct for Multinational Enterprises\*.



CSR Council, Local Resident Member  
Edgardo Bolipata

\* Principles and standards member states have agreed on to encourage multinational enterprises, which have a great impact on the development of the world economy, to act responsibly. Created by the OECD in 1976, the code of conduct includes voluntary rules and standards for responsible business conduct in regard to labor standards, the environment, and a wide variety of other fields.

## TOPICS

### Aiming to achieve raw material procurement that promotes a recycling-based society— Kao's participation in the Roundtable on Sustainable Palm Oil (RSPO)

Kao has been promoting the manufacture of products using palm and coconut oil since before World War II. Such vegetable raw materials have gained attention in recent years as renewable resources, and global demand for them is rising. However, the development of palm plantations in response to growing demand has led to losses of biodiversity and made poor working conditions a more recalcitrant problem. In response, the World Wide Fund for Nature (WWF), a global NGO working to protect the environment; and some companies and other organizations came together to establish the Roundtable on Sustainable Palm Oil (RSPO) in 2004. The RSPO engages in active discussions of how to establish palm oil supplies that are sustainable from environmental and social perspectives. Believing that these discussions would contribute significantly to sustainable development, Kao formally joined the RSPO on April 4, 2007. Moving forward, we will take part in discussions with people representing various perspectives and redouble our efforts in social and environmental activities related to the production of palm oil.

### ● Distribution of hybrid coconut seedlings to farms at no charge

To advance the coconut industry, Kao performed research aimed at improving productivity through the development of new coconut varieties. That research did not produce commercialized results, but PKI uses the hybrids parent trees on the research farm to distribute seedlings to local farmers at no charge. Through fiscal year 2006,



it had distributed about 2,000 seedlings. That number of trees would be roughly equivalent to a 20ha coconut farm.

## Environmental Protection Activities

### ● Giant bamboo planting

Significant amounts of the giant bamboo growing wild within forests in Jasaan City have been cut down in recent years to make room for housing. To protect groundwater and for other purposes as well, PKI and local volunteers have been working to plant new stands of giant bamboo. This program was also held in 2006, when approximately 2,000 plants were planted.



### PKI Recognized for its Exceptional Community Activities by the Philippine Economic Zone Authority

Praising PKI for the breadth of its relationships with local communities and for its social contribution activities, the Philippine Economic Authority (PEZA) presented PKI with its "Outstanding Community Project Award" at its annual investors award ceremony in April 2007. This was the 12th awards ceremony held by PEZA. Other awards presented included "Outstanding Exporters," "Outstanding Employers," and "Outstanding Environmental Performers."



## List of Principal CSR Activities in Fiscal Year 2006

CSR Elements	Principal CSR Activities in Fiscal Year 2006	Principal CSR Results in Fiscal Year 2006	Page
Products and Services	<ul style="list-style-type: none"> <li>• <i>Yoki-Monozukuri</i></li> </ul>	<ul style="list-style-type: none"> <li>• Nikkei “Monozukuri” Prize awarded to Health Care Food Business</li> </ul>	See page 10
		<ul style="list-style-type: none"> <li>• Expanded fatty alcohols production facilities</li> </ul>	See page 12
Corporate Governance	<ul style="list-style-type: none"> <li>• To strengthen internal controls</li> </ul>	<ul style="list-style-type: none"> <li>• Inaugurated and implemented documentation promotion project</li> </ul>	See page 19
CSR Promotion	<ul style="list-style-type: none"> <li>• To increased internal CSR awareness</li> </ul>	<ul style="list-style-type: none"> <li>• Briefings held, reports distributed, etc.</li> </ul>	See page 20
		<ul style="list-style-type: none"> <li>• Assistance provided to those who want to see the movie, <i>An Inconvenient Truth</i></li> </ul>	See page 20
Compliance	<ul style="list-style-type: none"> <li>• To expand to the entire Kao Group</li> </ul>	<ul style="list-style-type: none"> <li>• Continued BCG introduction</li> </ul>	See page 21
	<ul style="list-style-type: none"> <li>• To increase employee awareness</li> </ul>	<ul style="list-style-type: none"> <li>• Created and tested e-learning tool</li> </ul>	See page 22
Risk Management	<ul style="list-style-type: none"> <li>• To strengthen risk management system</li> </ul>	<ul style="list-style-type: none"> <li>• Strengthened Business Continuity Plan</li> </ul>	See page 24
Product Quality Management	<ul style="list-style-type: none"> <li>• To take measures to comply with the Revised Consumer Products Safety Law</li> </ul>	<ul style="list-style-type: none"> <li>• Strengthened safety management system</li> </ul>	See page 26
	<ul style="list-style-type: none"> <li>• To strengthen comprehensive management of chemicals</li> </ul>	<ul style="list-style-type: none"> <li>• Introduced and extended new system to worldwide locations</li> </ul>	See page 27
Occupational Safety	<ul style="list-style-type: none"> <li>• To extend to the entire Kao Group</li> </ul>	<ul style="list-style-type: none"> <li>• Extended to the entire Kao Group continued</li> </ul>	See page 28
Consumers	<ul style="list-style-type: none"> <li>• To form partnerships with consumer organizations</li> </ul>	<ul style="list-style-type: none"> <li>• Participated in environmental exhibits, etc.</li> </ul>	See page 33
	<ul style="list-style-type: none"> <li>• To extend to overseas groups</li> </ul>	<ul style="list-style-type: none"> <li>• Held meeting for managers in charge of consumer consultation in the Asian region</li> </ul>	See page 33
Employees	<ul style="list-style-type: none"> <li>• To promote diversity</li> </ul>	<ul style="list-style-type: none"> <li>• Took measures to comply with the Law for Measures to Support the Development of the Next Generation</li> </ul>	See page 37
		<ul style="list-style-type: none"> <li>• Introduced the Senior Partner System</li> </ul>	See page 38
Suppliers	<ul style="list-style-type: none"> <li>• To promote CSR procurement</li> </ul>	<ul style="list-style-type: none"> <li>• Created CSR procurement standards and started implementation</li> </ul>	See page 41
Shareholders/Investors	<ul style="list-style-type: none"> <li>• To increase dividends</li> </ul>	<ul style="list-style-type: none"> <li>• Increased dividend for 17 consecutive years</li> </ul>	See page 42
	<ul style="list-style-type: none"> <li>• To improve General Meeting of Shareholders</li> </ul>	<ul style="list-style-type: none"> <li>• Introduced electronic voting</li> </ul>	See page 42
Local Communities	<ul style="list-style-type: none"> <li>• To support civil activities</li> </ul>	<ul style="list-style-type: none"> <li>• Strengthened “Kao Creating Forests for Everyone” program</li> </ul>	See page 44
Environment	<ul style="list-style-type: none"> <li>• To achieve environmental targets</li> </ul>	<ul style="list-style-type: none"> <li>• Achieved zero emissions at all domestic production plants</li> </ul>	See page 52
		<ul style="list-style-type: none"> <li>• Joined RSPO</li> </ul>	See page 15



# CSR Management System

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RC (Environmental, Safety) Management  
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As it endeavors to achieve sound growth, Kao is working to build a corporate governance system that will result in highly transparent management, so that it can meet its responsibilities to society.

## Corporate Governance System

### Basic concept and management structure

The basic concept underlying Kao's corporate governance calls for the development of management and internal control systems that promote the realization of highly efficient, sound, and transparent management that, in turn, will support continuous increases in corporate value. The strengthening of management and internal control systems is an important management concern, and we implement measures necessary to act on it.

In fiscal year 2002, Kao introduced an executive officer system to promote the separation between executive and supervisory functions within the framework of directors and auditors. We also began appointing outside directors to strengthen supervision of management.

As of the end of March 2007, Kao's management was composed of a 15-member Board of Directors, including two outside directors and the Chairman of the Board of Directors, who has no representative rights and is not involved at an executive level, and 23 Executive Officers, including 11 who serve concurrently as members of the Board of Directors.

### Appointment, remuneration, and evaluation of Directors

Kao strives to secure transparency with regard to director appointments and remuneration. Specifically, we have established the Committee for the Examination of the Nominees for the Chairperson of the Board of Directors and the President, which is composed of only outside directors and outside corporate auditors, to provide opinions on the qualification of nominees for the Chairperson of the Board of

Directors and the President.

We have also established our Compensation Advisory Committee, which is comprised of representative directors, the Chairperson of the Board of Directors, and outside directors, to annually review compensation for currently serving directors and executive officers prior to compensation revisions. We have implemented a stock option plan to align directors and executive officers interests with those of shareholders, and linked compensation to performance, based on EVA (Economic Value Added) and other standards.

Kao regularly has its executives undergo 360° evaluations to determine whether they have the necessary competence as a leader and to help them improve themselves based on the opinions of those who work above, beside, and below them.

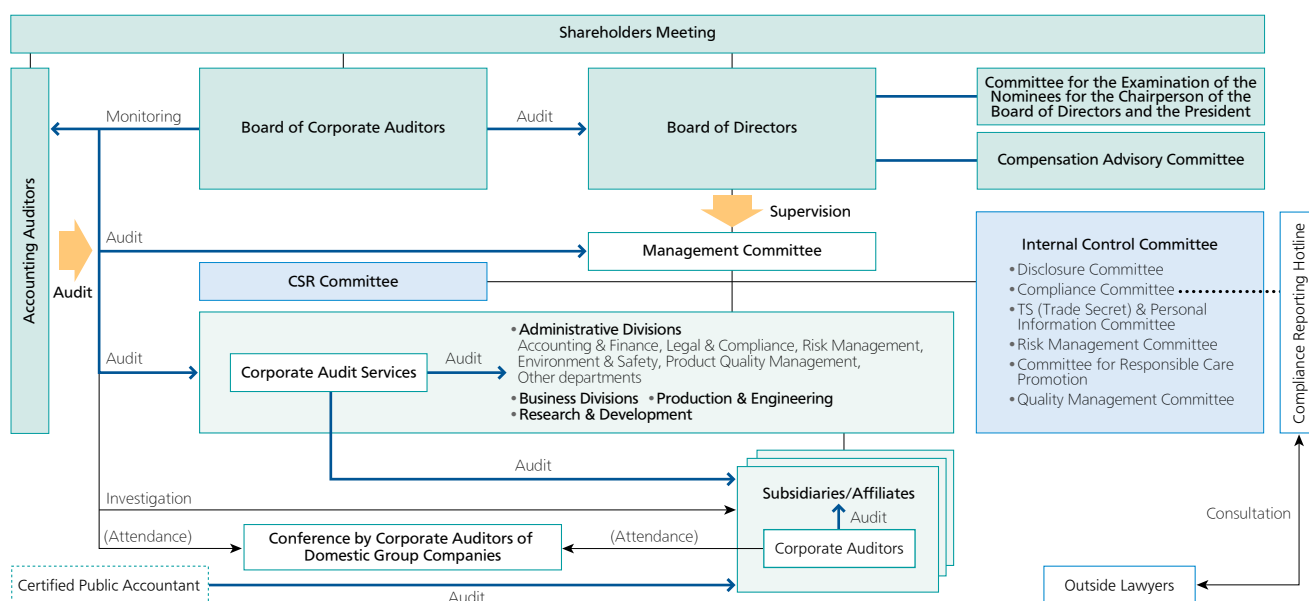
### Functions for monitoring and supervising management and business activity

Kao has established its Corporate Audit Services to examine the appropriateness of operational processes and the adequacy and efficiency of management, at Kao Group entities including domestic and overseas affiliates.

Four corporate auditors, including two from outside the company, worked to improve auditing effectiveness and efficiency by regularly exchanging views with representative directors, attending Management Committee and other important meetings, participating in regular meetings with the corporate auditors of domestic group companies, and sharing information with the Corporate Audit Services and the accounting auditor, as necessary.

In fiscal year 2006, Kao performed audits to determine compliance with internal rules, and audited exports as called for by the Foreign Exchange and Foreign Trade Law.

## Corporate Governance Structure



## Internal Control System

### Creating an internal control structure

Kao established its Internal Control Committee (chaired by the President and CEO) to establish basic internal control policies, and discuss and determine operating plans.

Six associated committees comprising the Internal Control Committee employ the PDCA cycle to promote internal control from the perspectives of information disclosure, compliance, confidentiality of trade secrets and personal information, risk management, responsible care, and quality management. Executives who comprise these six committees as key members also serve in the secretariat of the Internal Control Committee, which provides overall internal control oversight. This committee also includes the heads of divisions handling legal & compliance, environmental & safety matters, product quality management, risk management, human capital development, accounting & finance, information systems, and corporate audits services.

We formulated our Basic Policies on the Development of Internal Control in May 2006 and are now working to implement them.

### Documentation promotion project launched

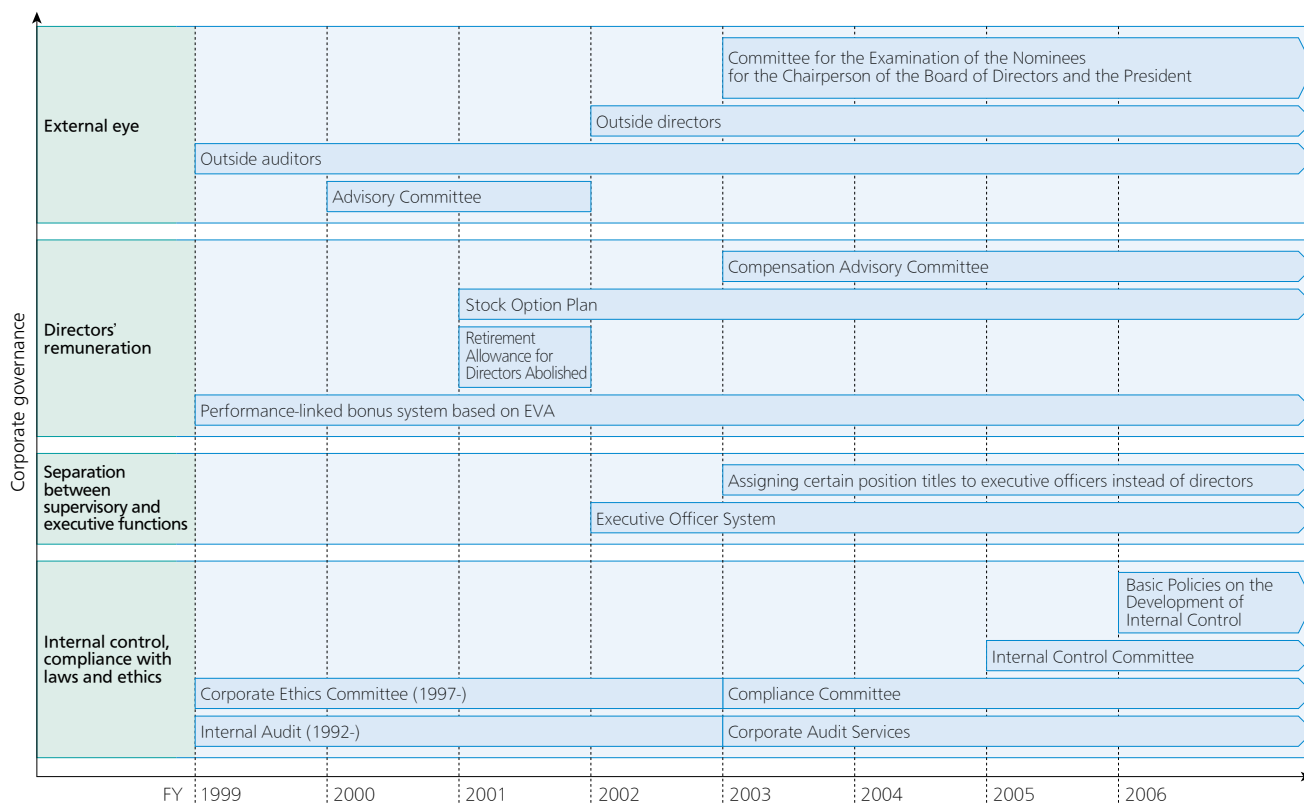
In 2006, Kao launched its Project to Promote the Documentation of Internal Control as a step toward constructing an internal control system for financial statements. The purpose of this project is to enhance financial statement reliability and management transparency and help ensure that shareholders and other investors are not misled. This project will document the primary business activities of principal Kao Group companies, identify business process risks and controls, and determine whether business activities are being performed properly.

In fiscal year 2006, attention was focused on documenting the primary business activities of Kao and its principal domestic affiliates. Documentation evaluations and improvements will be implemented during the first half of fiscal year 2007. Documentation of the business activities of principal overseas affiliates has also been started. Preliminary examinations for internal control audits are scheduled in the second half of fiscal year 2007 in order to start performing internal control audits during fiscal year 2008.

**HP** Kao's Corporate Governance

<http://www.kao.co.jp/en/company/governance/>

## Continuous Management Reform



Kao has established CSR Committee and CSR department, and taken other steps to create companywide organizational structures to continuously and systematically promote CSR as a Kao Group activity.

## CSR Promotion

### Basic policies and promotion system

Kao established its CSR Committee and CSR Department to continue CSR activities at the group level. The CSR Committee meets bimonthly to consider CSR issues facing the entire company, and individual divisions address issues at their level. Individual divisions, working around a core of company activities based on The Kao Way, continuously strengthen and enhance a wide variety of activities like the building of organizational structures that make the most of the varied abilities of employees, promotion of CSR activities to supply-chain companies, and initiatives to protect the global environment.

As part of its efforts to meet social responsibilities at an international level, Kao participated in the United Nations' Global Compact\*, which it continues to support. Every year, we conduct a Global-Compact-based survey among Kao Group companies throughout the world. In the survey for fiscal year 2006, no problems, like those involving child labor, were revealed.

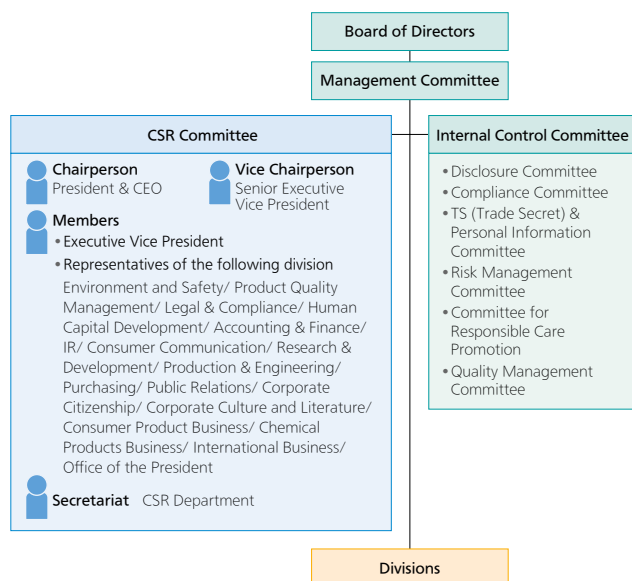
Looking toward the future, we will undertake measures to promote the adoption of Kao's basic CSR policies and initiatives among domestic and overseas Kao Group companies and affiliates.

#### \* Global Compact

The Global Compact is a set of 10 principles addressing matters of human rights, labor, the environment, and corruption, and is supported by companies acting as global citizens, throughout the world. The concept of the Global Compact were first proposed by former Secretary-General of the United Nations, Kofi Annan, at the World Economic Forum, held in Davos, Switzerland in 1999.

 Global Compact  
<http://www.unic.or.jp/globalcomp/>

### CSR Structure (As of March 31, 2007)



## Promoting Activities Designed for the Participation of All Employees

Kao believes that fulfilling CSR requires that all employees be aware of CSR and that activities focus on specific conditions and issues.

Based on that position, we held employee briefings aimed at enhancing and deepening understanding of CSR. These briefings, which took place in fiscal year 2006, defined CSR, explained Kao's CSR, and discussed what individual divisions and employees should do.

### CSR awareness within the company

Kao explains CSR in training that employees undergo when they are newly hired, promoted, etc.

In fiscal year 2006, we held additional 21 CSR seminars primarily in production and research divisions.

Furthermore, to advance CSR awareness activities for overseas affiliates, we implemented local CSR training, using Kao in Thailand as a model, and had a CSR seminar in the training for leaders of overseas HR departments, and other training held for Group employees from Asian countries. To boost awareness of the global environment, we provided employees with tickets to see the movie, *An Inconvenient Truth*, and held a screening for all company officers.

### CSR Report distribution, survey implementation

In fiscal year 2006, Kao distributed its CSR Report to its 15,000 domestic Group employees and 1,500 overseas Group employees, as it did in the previous year, to help Kao employees understand CSR activities from an overall perspective. We also asked all employees in supervisory positions to encourage subordinates to read the report.

At the same time, to gauge employees' CSR awareness and to gain hints for improving our CSR Report, we conducted a survey on the report. Among the approximate 1,000 responses were comments like "the report provides a good overview of the entire company's activities," "it made me feel that CSR activities are important for gaining the trust from society," and "the report was much improved over last year's." However, we also received comments saying, for example, that "the report is too long" and that we should "make it easier to read."

While over 80% of respondents said, "I understand Kao's CSR," there were also those who said that they "feel it is necessary to make CSR a more prominent fixture in daily activities." Bringing CSR down to the level of daily work, therefore, is an issue that we must address moving forward.

Working from the foundation of “Integrity” set forth in The Kao Way, Kao practices conduct in compliance with laws and ethics, and responds to stakeholders to earn their trust through business activities that are sound and honest.

## Basic Concepts and Promotion System

As a result of a string of corporate scandals in recent years, consumers have come to view companies with an increasingly skeptical eye. At Kao, where The Kao Way sets forth “Integrity” as one of our values, we conduct ourselves in ways in compliance with laws and ethics and have clearly stated in writing that we will respond to the respect and trust of all of our stakeholders through business activities that are sound and honest. As a code of conduct in the daily activities, we have created Kao’s Business Conduct Guidelines (BCG), based on references to documents like Nippon Keidanren’s Charter of Corporate Behavior and the Global Compact.

### Kao’s Business Conduct Guidelines

1. Ensure the Safety and High Quality of Products
2. Thoroughly Consider the Environment and Safety
3. Maintain Fair and Honest Transactions
4. Respect Employees’ Individual Human Rights and Diversity, and Maximize Their Potential
5. Pursue Profitable Growth and Accommodate Shareholders’ Expectations
6. Maintain a Fair, Open and Exemplary Corporate Position
7. Strictly Manage Information and Assets
8. Contribute to the Enrichment of Society through Activities that Make a Social Contribution
9. Respect Cultures of Individual Countries and Observe Laws and International Rules When Conducting Business Activities
10. Draw a Distinct Line between Business and Private Matters
11. Executives and Managers Shall Acknowledge Responsibilities

 Entire text of Kao’s Business Conduct Guidelines  
<http://www.kao.co.jp/en/company/guidelines/>

### Compliance promotion system

Kao has established its Compliance Committee, which is chaired by the Executive Vice President and includes as members representatives of divisions and affiliated companies. The Compliance Committee institutes and revises the Kao BCG, implements activities that promote the penetration and adoption of corporate ethics, operates the compliance hotline, reviews and monitors reactions to hotline reports, and reports important matters and its decisions to the Board of Directors.

To help ensure thorough compliance, the Compliance Committee has created its own “legal expert” system. Legal experts are employees who have a firm grasp of domestic laws related to specific businesses. They closely monitor information on the course of legal revisions and, when necessary, promote the dissemination of information through means such as internal seminars. Legal experts are appointed

to address matters related to particular laws and their names are disclosed within the company. When employees, in performing their jobs, must decide whether something is legal or not, they turn first to the legal expert. Legal experts also support the work of Directors by performing checks to determine whether Kao business activities are being performed within the bounds of the law and company rules. As of the end of March 2007, Kao had 84 legal experts handling matters with regard to 247 laws.

In fiscal year 2006 legal experts held internal seminars on laws and regulation related to topics like comprehensive chemical management, the Export Trade Control Order, the Pharmaceutical Affairs Law, the Revised Consumer Products Safety Law, the Act Concerning Protection of Personal Information, and the Securities and Exchange Law.

In fiscal year 2006, there were no significant legal violations committed in pursuit of the Kao Group’s business activities.

### Ensuring compliance with regard to fair trade

The Kao BCG require that all transactions be conducted with fairness and honesty. Additionally, the following major checks are performed in each process from product development to marketing.

- Product label checks by each division in development process
- Advertising review meetings attended by not only members of the media and creative division but also representatives of divisions ranging from product development and marketing.

### Compliance reporting hotline expansion and enhancement

Kao has created several compliance hotlines for employees to report business activities that may include legal or ethical violations. Internal hotline are staffed by the Kao Compliance Committee’s administrative staff, while external hotlines by lawyers and other specialist. These services are available to all Kao Group employees in Japan, but also receive calls from suppliers and other outside parties. The identities of hotline callers are strictly protected. Information received is checked with the relevant division and any violations are corrected.

In fiscal year 2006, an average of about 10 hotline calls were received per month, and there were no reports of serious legal violations.

Kao is also considering introducing a global helpline for overseas Kao Group employees. Specifically, Kao Brands Company and its subsidiaries are planning to use an outsourcing service in implementing a system that will allow employees to express their concerns in their mother tongue 24 hours a day, 365 days a year. This test will take place in fiscal year 2007. Pending the results of this test, help lines will be introduced for the entire overseas Kao Group in the future.



## Compliance Auditing and Monitoring

At Kao, internal compliance audits by Corporate Audit Services, FIND employee opinion surveys (See page 38), self-assessment by Compliance Committee members in each division, and compliance awareness self-check exercises by training participants are implemented regularly.

### Test of e-learning tools started

Kao has prepared e-learning tools to ensure a thorough understanding of the Kao BCG among all employees. In fiscal year 2006, we created a pilot program with content employees would find relevant and easy to grasp in a short amount of time, and we performed testing that will lead to actual implementation in fiscal year 2007. Our goal is to reinforce understanding of the Kao BCG by eventually having all employees use e-learning tools and take the associated tests.

## Protection of Intellectual Property Rights

Intellectual property rights are an important underpinning of Kao's business activities. At Kao, we promote the acquisition of intellectual property rights in ways that are consistent with our business activities, and take rigorous action, as permitted by law, against violations of our intellectual property rights. We also, however, take steps to avoid violating the intellectual property rights of others.

To further the smooth implementation of *Yoki-Monozukuri*, Kao has established its Intellectual Property Center to handle patents and utility models, its Trademark Department to oversee trademarks and copyrights, and other dedicated organizations in an effort to protect our intellectual property rights. Our Trademark Department also deals with the problem of counterfeit goods in Asia.

Additionally, our R&D, marketing, and other divisions work closely with our Intellectual Property Center and Trademark Department to secure our intellectual property rights and avoid violating those of others by identifying technologies that are common knowledge and intellectual property belonging to others. These efforts get underway at the earliest stages of a new product development project.

## Information Security and Protection of Personal Information

To promote compliance with the Act Concerning Protection of Personal Information and other similar laws, Kao has established its Guidelines on Handling Trade Secret Information, Guidelines on Handling Personal Information,

and IT Security Guidelines based on its information Security Policy. Furthermore, as a part of our efforts to strengthen our internal controls, members of our Trade Secret (TS) & Personal Information Committee, divisional employees responsible for protecting trade secrets, and personal information management supervisors each perform their role in ensuring thorough information security management. Kao trains and educates these personnel on an ongoing basis.

Regarding the protection of personal information, Kao, in connection with its business activities, collects personal information on many people. These people include consumers responding to sales campaigns, consumer monitors, and people who contact our Consumer Communication Center, and we strictly manage their information in accordance with guidelines set forth by the Ministry of Economy, Trade and Industry and others. When we outsource work involving the handling of personal information, we enter into a contractual agreement with the service provider, conduct audits, and take other steps consistent with thorough supervision. Concerning the protection of employees' personal information, we practice appropriate management in accordance with guidelines provided by the Ministry of Health, Labour and Welfare.

### Implementation of Voluntary Patrols

In July and August of every year, divisional members of our Trade Secret (TS) & Personal Information Committee and personal information management supervisors conduct self-patrols to examine the conditions under which trade secrets and personal information are being managed in their divisions. Issues they identify are discussed in the Trade Secret & Personal Information Meeting held in September and deficiencies are set as problems to be resolved during the coming year. In fiscal year 2006, we identified management deficiencies at an outsourcing service provider, so we strengthened measures like using our auditing process to request improvements.

### Regarding the Leaking of Cosmetics Sales Information

In January 2007, it became clear that the confidential information of a cosmetics sales company Kao deals with was leaked on the Internet. The leak occurred when an employee took information home to work with it on his own personal computer, which turned out to be infected by a computer virus in a file exchange program. Kao took this information leak very seriously and moved to prevent a recurrence by, for example, taking steps to ensure that employees of Kao Group companies thoroughly understand internal rules and rules on handling trade secrets and personal information.

Based on Kao's Risk Management Policy and a matrix-style organization of business divisions and functional divisions, we set a theme for each year and strengthen our activities.

## Basic Concept and Kao's Risk Management Policy

To implement Kao's corporate philosophy of *Yoki-Monozukuri*, with thorough consideration of product quality & safety, occupational safety, and the environment, we must establish policies for dealing with every type of envisioned risk we face throughout our business operations, lessening the frequency of risk emergence and reducing the risk impact, taking other appropriate management measures, and minimize damage resulting from risks that are realized.

Working from this concept, Kao, based on its Risk Management Policy, manages and responds to risks, giving highest priority the human lives of our customers, business partners, local residents, employees, and others, and then to protecting the environment, continuation of operations, and protection of assets, in that order.

## Risk Management System

Kao's Board of Directors oversees and regularly reviews the entire company's risk management system, and determines basic policies for major risks.

Business condition, market environment, new product development, overseas business, raw material market, human

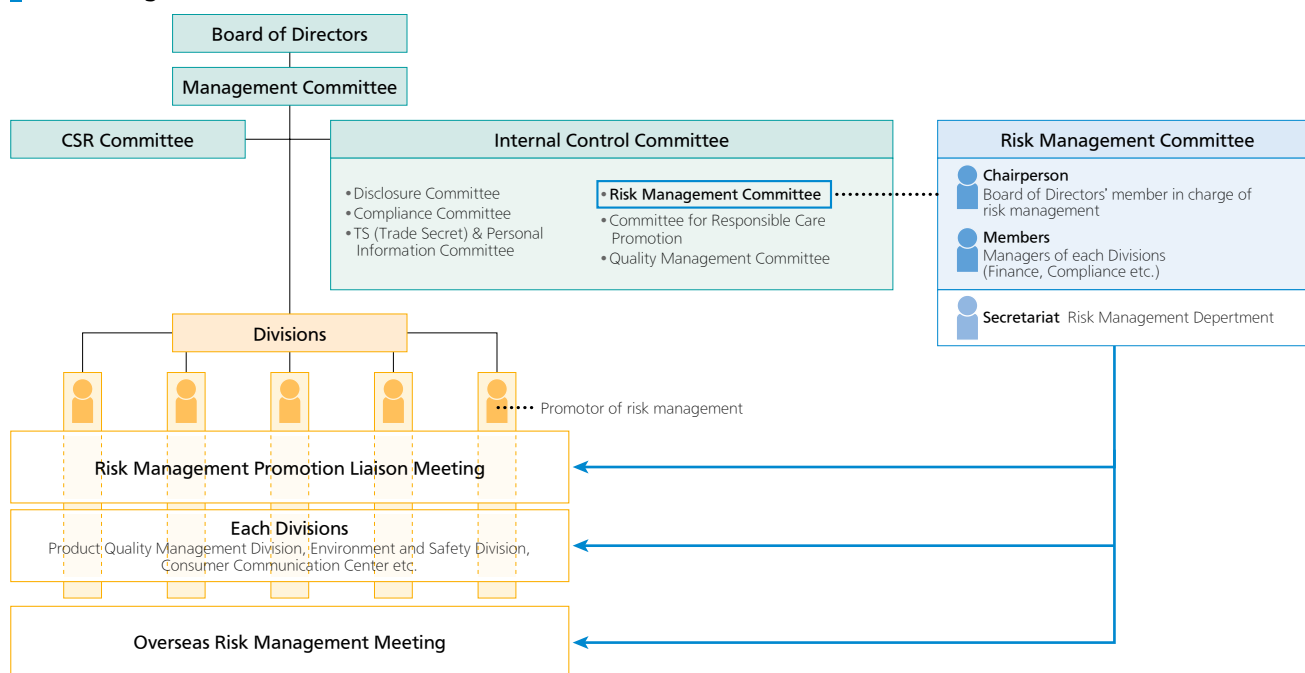
resource development, and other management strategic risks Kao may face in its business activities are subjected to analysis and the development of countermeasures in related divisions. When necessary, the Management Committee and Board of Directors discuss these risks and make decisions.

Each division designates a person to be responsible for risk management, and identifies and assesses risks, considers avoidance and mitigation measures, devises response approaches and takes other appropriate risk management steps to help responsible divisions identify risks associated with disasters/accidents, product quality, and other problems, take measures to reduce the frequency of emergence, and minimize damage should a risk to be realized. To standardize risk management methods, risk management supervisors hold Risk Management Promotion Liaison Meetings three times a year and report on the status of risk management and risk countermeasures to the President and CEO, and Board of Directors, as necessary.

Additionally, divisions handling product quality, environmental, information systems, and other matters affecting the entire company practice risk management from a similar perspective through a matrix-style organization.

To address operational risks at overseas businesses, which account for one-fourth of Kao's consolidated sales, Overseas Risk Management Meetings are held every other month, risk information is shared, and systems have been put in place to train Japanese personnel assigned overseas and communicate through specified networks during emergencies.

### Risk Management Structure



### Activities of the Risk Management Department

Kao has established its Risk Management Department, which employs the PDCA risk-management cycle to determine the status of risk management in each division, provide support for improvements, and strengthen risk management from cross-division, cross-group perspectives.

The Risk Management Department regularly holds Risk Management Committee meetings attended by officers and Risk Management Committee members, reviews the planning, implementation, and reporting of risk management activities in individual divisions on a monthly basis, and works to strengthen risk management activities by sharing information with related divisions. The Risk Management Committee became an associated committee of the Internal Control Committee (See page 19) as of September 2005.

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### Major Risks and Responses to Their Realization

Kao identifies accident and disaster, product defect, and other major risks, and has devised and promotes various response systems and activities placing human life above all else.

In fiscal year 2006, we established “improvement of risk prevention and initial response for accident, disaster and product quality,” and “formulation of a Business Continuity Plan (BCP\*)” as major themes for minimizing damage should a risk be realized, and enhanced our activities accordingly. A BCP consists of business impact analyses, and the formulation, implementation and management of a plan for restoring and continuing operations when a major disaster occurs. We continue to consider business continuity planning from perspectives like prioritizing operations, considering possibilities for using other plants for production, establishing a chain of command, and securing substitute facilities.

\* BCP Business Continuity Plan

### Emergency and disaster response

Kao has prepared various measures for responding to earthquakes and other natural disasters, and accidents and other emergency situations.

For example, to confirm the condition of employees in the aftermath of a natural disaster, we have not only created communication networks for each work location but also implemented our Personal Safety Information Registration System to address conditions related to disasters that occur at night and on days off. We have also prepared several days' stockpiles of food/water and bedding to allow employees to stay at their places of work when they cannot return to their homes after a disaster.

More information on measures such as these and on specific procedures is included in our BCP.

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### Survey and Quantification of Major Risks

In fiscal year 2006, we carried out surveys of, and quantified, major risks on a division-by-division basis, under the theme of “Promoting Companywide Risk Management Activities.” Specifically, we developed scenarios based on the realization of various risks, like that of a plant stoppage due to a natural disaster, and estimated damage and other figures. We reflected factors, like significance and the size of monetary amounts involved, in the company's risk map. Furthermore, we held training for notification to the Disaster Prevention Headquarters and for data input to Emergency Contact and Safety Confirmation System.

In addition, continuing from fiscal year 2005, we pushed forward with the development of BCPs at individual facilities, and strengthened systems for responding to infectious diseases like bird flu and other overseas risks.

Kao has built a companywide quality management system covering every stage from product development to marketing, and enhanced our ability to respond to a quality problem should it arise.

## Basic Concept of Quality Management Activities

Kao provides several thousand products ranging from chemical products to consumer products for consumers. For these products, Kao uses more than 10,000 raw materials. So that all of these products can be used by customers/consumers with confidence, we established our Policies for Quality Management Activities, the first among which is that, "consumers/customers decide on the quality of the products," based on the "Consumer Driven" Principle in the Kao Way.

### Policies for Quality Management Activities

1. Consumers/customers decide on the quality of the products
2. Providing products that users wish to continue to use
3. Ensuring safe usage for consumers/customers
4. Legal compliance
5. Transparency and accountability

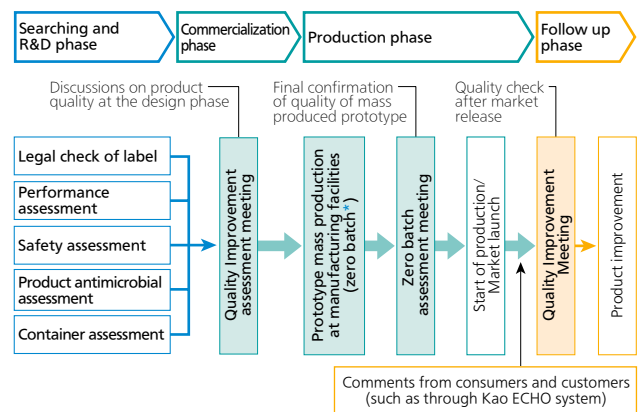
## Quality Management System

The Quality Management Committee, which is part of the Internal Control Committee, promotes companywide quality management activities that confirm the effectiveness and reliability of its activities. The Product Quality Management Division, which independently bears quality management responsibility within the company, oversees and promotes activities. The Quality Management Committee, which is composed of the officer responsible for the Product Quality Management Division and representatives selected from relevant divisions, discusses and determines basic quality management policies and measures, and confirms and checks items discussed and activities undertaken in each division's Quality Management Meetings and Quality Improvement Study Meetings.

## Companywide Quality Management Activities Covering Every Stage from Product Development to Post-launch

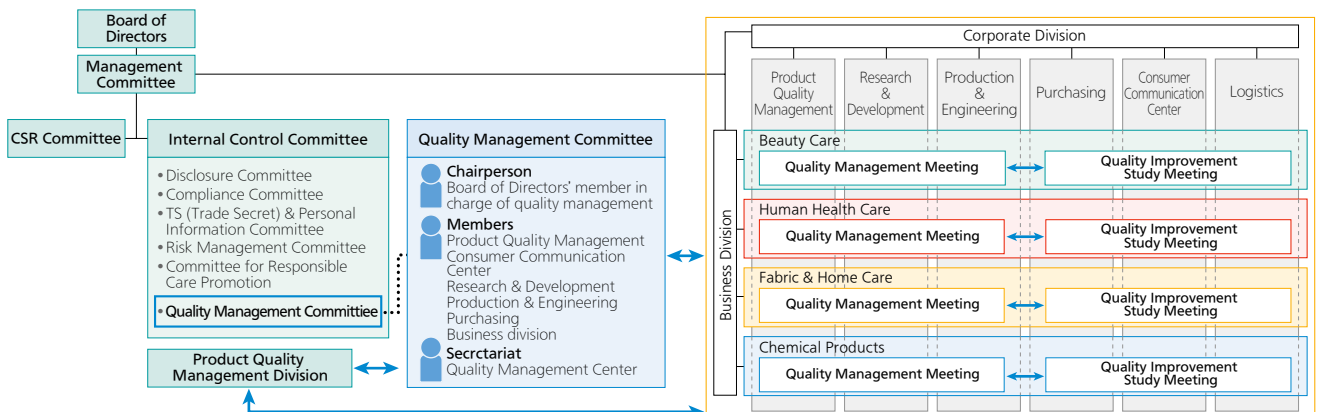
As part of its effort to assure product quality from a wide array of perspectives, including raw materials, product usage methods, product labels, and social responsibilities, Kao holds companywide meetings to consider topics like safety, product antimicrobial protection, product containers, and quality improvement at every stage from research to product development, production, distribution, marketing, and disposal. Through these activities, we endeavor to deliver complete safety and confidence by strictly scrutinizing whether we can gain a customer's faith and support once he/she has come to know the product, use it, store it, and dispose of it.

### Quality Management Flow



\* **Zero batch** Experimental manufacturing of a product as a final conformation under actual conditions using the actual manufacturing facilities and containers.

### Quality Management Structure



### Companywide Product Safety Management System

Development and provision of high-quality products with a focus on safety is at the very heart of *Yoki-Monozukuri*. Regarding the safety of products and raw materials, we establish strict safety standards, practice scientific risk assessments, and evaluate and consider various issues related to actual usage and foreseeable misuse, and sell only products we can confirm to be safe.

There are, nevertheless, unimaginable accidents that may occur, for example, because warnings on labels were not heeded. Furthermore, on May 14, 2007, the revised Consumer Products Safety Law took effect in response to accidents involving water heaters and other products in 2006. For its part, Kao has created its Companywide Safety Management System, which is overseen by the Product Quality Management Division, to ensure that our responses to safety-related problems or accidents place top priority on consumer safety and peace of mind, emphasizing the physical recovery of those involved above all else, and permit the rapid implementation of measures for identifying causes and preventing recurrences.

Moving forward, we will continue to place top priority on human safety as we pursue strict safety assessments, the provision of safety warnings and other appropriate information, and other necessary actions.

#### Basic Principle of Safety Assessments

- Assess and ensure the safety of both raw materials (the composition) and finished products.
- Assure safety to human beings and the environment in relation to products under normal conditions of use and foreseeable misuse.
- Use the most innovative technologies and expertise available at the time of assessment.
- Discuss and confirm legal compliance and product safety from the social science perspective.

#### Development and establishment of alternatives to animal testing

To protect animals, Kao, in cooperation with the national government and other companies, has been working to develop alternatives to animal testing. Furthermore, in view of the EU's phase in of sales restrictions on cosmetics developed

with animal testing, due to begin in 2009, we have redoubled our research and development efforts in this area in recent years. We are also actively presenting our research results at academic conferences and in academic papers, so that anybody can use them.

In fiscal year 2006, we, in conjunction with seven cosmetics companies and the National Institute of Health Sciences, began to put into practical use a substitute test for the presence of cosmetics allergies. This test uses basic technology developed together with Shiseido Co., Ltd. Additionally, Kao and Kanebo Cosmetics' safety research laboratories have jointly developed a method for quickly performing safety tests without using test animals. (See page 30)

### Quality Management for Health Care Products

In pursuit of health functionality based on human health care research, Kao is developing a health care products business that will provide functional foods that can be consumed with a sense of security as part of a regular diet. Regarding quality management for these foods, we are focusing on the following two initiatives.

- In product development, we are performing product effectiveness and safety research not only internally but also in cooperation with external nutrition science institutions and medical specialists, and performing numerous evaluations before launching new products.
- We practice thorough quality management in production and processing, and implemented quality management through traceability spanning everything from procurement of Original materials\* to consumption.

#### \* Original materials

Refers to primary agricultural, livestock and marine products themselves. Soybeans would be an example in the case of cooking oil.

#### Traceability and auditing of food raw materials

Kao has established a traceability system that can trace all raw materials. With this system, we can trace, by product lot number, not only the countries of origin but also compliance with laws and regulations, and original materials. After obtaining traceability information from our raw material suppliers, we enter into quality agreements taking the form of certificates of product specifications.

Furthermore, we confirm the contents of these agreements and details of management systems through regular audits and meetings with raw material suppliers.



## Management of product “best-before” dates

Kao determines food product “best-before” dates after building in an adequate safety margin based on the results of various types of storage tests, and setting periods that permit consumers to enjoy its products without experiencing problems in quality or taste.

So that customers can enjoy our products of the “best-before” date, we focus on managing freshness, which includes management of “best-before” dates for raw materials, in production and distribution. Specifically, we make it a rule to deliver products to retailers no later than the date that is one-third of the way between the production and “best-before” dates, and have built management and traceability systems based on production lot numbers.

\* Kao issues a pamphlet titled, *Kao's Quality Management Activities*, which provides details on its quality management ideas and management systems.

## Product Recalls

### Learning from the July 2006 recall

In July 2006, it became clear that trial-use samples of *Econa Healthy & Healthy Cooking Oil* (48 bottles) past their “best-before” dates had been mistakenly distributed to customers at the gift section of an Osaka department store. Kao voluntarily recalled these products based on its rules for handling emergency/major product quality problems. Kao has always paid careful attention to the management of product expiration dates, but our management of sample “best-before” dates was insufficient. Learning from this regrettable incident, Kao has now made it a rule to distribute samples no later than the date that is two-thirds of the way between the production and “best-before” dates, and has strengthened its sample management system to include measures that tighten distribution records and inventory management.

## COLUMN

## Comprehensive Management System for Chemical Substances

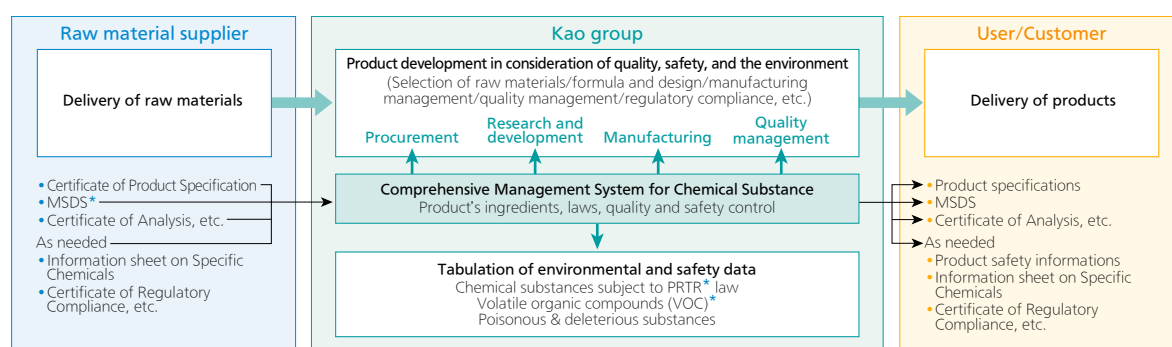
In 2001, Kao began building its Comprehensive Management System for Chemical Substances, a database built using the Master Index\* of the Kao Group's standardized raw material codes. This system allows us to gradually add chemical registrations, incorporate the latest regulatory (chemical, pharmaceutical, food, and environmental) information, share information with other divisions, including those involved with quality management, and, thereby, confirm product safety and legal compliance at any stage from development to distribution. Regarding raw material traceability, we can instantly determine what went into making the raw materials for a particular product, whether raw materials comply with safety standards and are legal, and whether internal management standards have been met.

In recent years, as our business activities have become more global and we have become involved in broader areas of business, we have seen regulatory changes throughout

the world. It has therefore become necessary to implement more sophisticated quality management methods and take other measures to strengthen our systems for addressing changes in our business environment. In 2006, Kao developed the New Product Development Support System, which can be used for multiple purposes at all stages, beginning with product R&D. Working from a base of existing functions, this system makes it possible to comply not only with chemical regulations in Japan but also with those in other countries, and to create appropriate labels. It also incorporates a full range of quality and labor safety data. This system has made it possible for us to meet the demands of accelerated R&D and globalization. The Kao Group has positioned this system as a key support element for *Yoki-Monozukuri*.

\* The Master Index has a hierarchical structure consisting of four levels: Consumer products, chemical products, raw materials, and ingredients.

## Overview of Kao's Comprehensive Chemical Substance Management



\* MSDS/PRTR/VOC See page 55

Consistent with the ideas underlying the chemical industry's Responsible Care (RC) self-management activities, Kao manages all of its business activities from environmental and safety perspectives.

## Basic Policies for Environmental and Safety Activities

Kao pursues activities consistent with the ideas underlying the chemical industry's Responsible Care (RC) self-management environmental and safety activities to secure the safety of all stakeholders throughout the business cycle (product development, production, distribution, marketing and disposal) and protect the environment.

These activities are pursued by our Research & Development, Production & Engineering, and other divisions based on the five RC activity objectives\* and one we added, communication with society.

### \* Five RC Activity Objectives

Environmental conservation, Process safety and disaster prevention, Occupational safety and health, Chemical and product safety, Distribution safety

### Philosophy Regarding the Environment and Safety

Kao is committed to a responsible approach to the environment and safety throughout the entire lifecycle of products, from product development, production and distribution, to consumption and final disposal. At the same time, Kao endeavors to contribute to sustainable development and a higher quality of life for people all around the world.

### Policies Regarding the Environment and Safety

1. Maintain employees' health and safety and improve operational safety
2. Develop products with attention to the environment and safety
3. Save resources and energy and reduce waste
4. Promote human safety in the community and take a responsible approach to environmental conservation
5. Comply with laws and internal controls
6. Provide adequate training
7. Conduct evaluations
8. Disclose information and improve credibility in the community

HP Philosophy & Policies Regarding the Environment and Safety (only available in Japanese)

<http://www.kao.co.jp/corp/ecology/>

## Management Structure

To raise the level of self-management activities undertaken by individual divisions, Kao holds meetings of its Committee for Responsible Care Promotion every December. The committee is chaired by the officer responsible for the Environmental and Safety Division and includes representatives from each division as members.

The Committee for Responsible Care Promotion discusses: 1) Initiatives that support each division's activities by reinforcing understanding of the RC philosophy, enhancing management systems, etc.; and 2) Objectives for the following year's activities based on a consideration of the results of each October's internal audit.

The RC Promotion Planning Meeting is held in March of each year to discuss plans submitted by each division. Implementation of these plans leads to further improvement. The March 2007 RC Promotion Planning Meeting included the participation of a new member of the Kao Group, Kanebo Cosmetics, which reported on its fiscal year 2006 activities and discussed its fiscal year 2007 plans.

The Committee for Responsible Care Promotion became an associated committee of the Internal Control Committee (See page 19) established in September 2005.

### • Environmental management

Kao's environmental standards, rules, and system include the following: CSR Procurement and Green Purchase standards, Comprehensive Management Standards for Chemical Substances, Standards for Environmentally Conscious Design and Operative Provision, 5 Principles of Product Development, Product Safety Study Meetings, and the Environmental & Safety Data Management System.

### • Safety and disaster prevention management

In preparation for major disasters and accidents, Kao has established its Process Safety and Disaster Prevention Rules. To provide specifics for disaster prevention and response activities, we have created our Disaster Prevention Guidelines and Relief Aid Supply Outline. These guidelines and this outline provide policies and procedures for implementing local support activities and providing relief supplies, and allow us to rapidly provide assistance to areas according to their needs when a disaster strikes.

### • Occupational safety and health management

Together with the members of the health and safety committees

## Responsible Care Promotion Structure



established at each Kao facility, we are working to improve working environments and facilities, provide safety education, and undertaking other activities with the goal of eliminating occupational accidents. At factories, we are implementing equipment and facility risk assessments and chemical facility safety management based on the Occupational Safety and Health assessment System (OSHMS), as a part of proactive efforts to address sources of risk. We have also established the Occupational Safety Subcommittee within the Production & Engineering Division to discuss safety activities for all factories.

- **Chemical and product safety management**

Kao has created its Comprehensive Management Standards for Chemical Substances, Comprehensive Management System for Chemicals, and other rules and systems to manage everything from chemical raw materials to consumer products.

- **Distribution safety management**

To prevent distribution accidents and disasters, Kao has prepared Yellow Cards (See page 55) that it requires to carry. We also provide training and hold emergency response drills.

**HP** List of ISO and other certifications obtained  
<http://www.kao.co.jp/en/csr/report/addition/>

## Internal audits

Kao determines the status of RC activities and identifies issues to be addressed in each division through internal RC activity audits performed in October of each year. This information is subjected to a management review in each December's Committee for Responsible Care Promotion meeting and used to determine policies and targets for the coming year.

In fiscal year 2006, internal audits were performed on 28 divisions, six more than in fiscal year 2005, with results indicating no significant deficiencies.

To achieve even greater internal audit effectiveness, we plan to go beyond examining the thoroughness of management systems and actively review environmental performance improvement, safety, and other self-management activities.

## RC activity training

As required for RC activities, Kao provides ongoing training on ISO and occupational safety and health activities for both its own employees and employees of partner companies. Training is overseen by the Responsible Care Promotion Office and divisional supervisors. In the Production & Engineering Division, which requires broad environmental and safety knowledge, training is tailored to specific levels of personnel. Large numbers of engineers and operators from overseas production facilities participate in training sessions held in Japan.

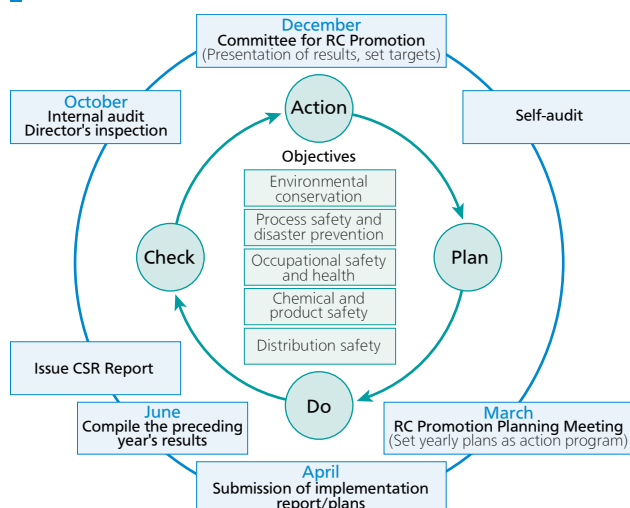
## Environmental & Safety Data Management System "Kanchan"

Kao has created its Comprehensive Management System for Chemical Substances (See page 27) and Environmental & Safety Data Management System "Kanchan" \* to help reduce its use of substances subject to the PRTR Law and volatile organic compounds, and decrease the number of occupational accidents.

These systems have allowed us to accumulate environmental burden data and reports of occupational accidents, and automatically compute figures like greenhouse gas emission volumes and occupational accident frequencies. They have also increased accuracy and speed with regard to management activities aimed at complying with the PRTR Law and MSDS issuance and management.

\* The Environmental & Safety Data Management System "Kanchan" automatically accumulates data on substances subject to the PRTR Law, PRTR substances specified by the Japan Chemical Industry Association, volatile organic compounds (VOCs), and poisonous and deleterious materials. Shared data includes energy consumption amounts; greenhouse gas emission volumes; SOx and soot & dust emissions volumes; soil and groundwater testing results; usage and emissions of substances subject to the PRTR Law; amounts of waste generated, emitted, and finally disposed of; occupational accident statistics, and traffic accident statistics.

## Annual Schedule for RC Activities



## Results of RC Internal Audit in FY2006

	Production & Engineering	R&D, Business, Corporate	Affiliates
No. of divisions audited	8	17	3
No. of questions	489	459	65
No. of items requiring continued observation	79	54	8
Average evaluation score (5-point scale)	4.9	4.7	4.5

## RC Training Provided to Production and Engineering Division in FY2006

Name of training course	Objectives	Number of participants
Techno school	Fostering of Operational engineers	22
School for Junior Engineers	Training for junior engineers	7
Management Basics	Training for production leaders	53

## Principal external evaluations and awards received during fiscal year 2006

## Principal Evaluations by External Institutions

Evaluating Institution/Publication	Title	Fiscal Year 2006 Results
Nihon Keizai Shimbun	Nikkei PRISM (Private Sector Multi Evaluation System)	27th
Newsweek (Japanese edition)	Newsweek Global 500 (Ranking of 500 companies based on CSR and financial performance)	22th (1st in Japan)
Nihon Keizai Shimbun	Employee Friendly Company	36th
Nikkan Kogyo Shimbun	Corporate Rating	5th
Nihon Keizai Shimbun	Nikkei Corporate Image Survey	13th in business people; 16th in general public segments
FORTUNE	Global Most Admired Company	7th in Household & Personal Products

## Principal External Awards

Award	Description
Kao Health Care Research Center receives 3rd Nikkei "Monozukuri" Award	<a href="#">See page 10</a>
Pilipinas Kao receives "Outstanding Community Projects Award" from the Philippine Economic Zone Authority (PEZA)	<a href="#">See page 15</a>
Wakayama Plant receives fiscal year 2006 Japan Cogeneration Center's Presidents Award (Industrial Division)	<a href="#">See page 54</a>
Healthya Water Receives 2006 Nikkei Excellent Product and Service Award	The Nikkei Excellent Product and Service Awards are presented annually by the Nikkei Shimbun for outstanding products and services in various categories. As a sports drink approved to bear the Food for Specified Health Use mark on its label, Healthya Water has opened up a new market and was recognized for revitalizing the sports drink market.
John Frieda LCG Treatment Receives the VVWD's Breakthrough Product of the Year Award	The new John Frieda product, <i>Luminous Color Glaze</i> , was recognized as the Breakthrough Product of the Year by "VVWD", fashion journal, which selects the most innovative product in the mass hair care division.
Laurier Active Guard Package Receives 45th JPC Apparel Division Award	The Japan Packaging Competition, which is sponsored once annually by the Japan Federation of Printing Industries, is Japan's largest packaging exhibition and a place for commercial packaging sold in the market to compete on excellence. Among awards presented in the packaging design field, these are the oldest and most influential.
Animal-Testing Alternative Developed by Kao and Kanebo Cosmetics received Golden Presentation Award by the Japanese Society for Alternatives to Animal Experiments	Kao and Kanebo Cosmetics developed a testing method that uses cultured cells to assess eye irritation. At the December 12, 2006 meeting of the Japanese Society for Alternatives to Animal Experiments, the effectiveness of that testing method was highly praised and the presentation describing it received the society's Golden Presentation Award.
Research on AGE Cleaning Agent Recognized as Outstanding by American Oil Chemist's Society	The nonionic surfactant AGE (Alkylglyceryl Ether) is used in <i>Family Kyukyutto</i> , a key component that has proved to have exceptional cleansing ability. The results of applied research on AGE were presented at the 97th AOCS Annual Meeting & Expo held in May 2006, and received the prize for most outstanding research in the field of surfactants and cleaning agents.
Paper on Technology that Makes Lipids Inside Hair Visible Recognized as Most Outstanding by Society of Cosmetic Chemists	Kao has developed technology that makes it possible to observe the lipids inside a hair. The paper describing that technology was published in <i>the Journal of Cosmetic Science</i> in the US, and presented with the Joseph P. Ciardelli Award for the year's best article on cosmetic-related technology.
Research on Preventing Obesity in Dogs Recognized as Outstanding by the Japanese Society of Pet Animal Nutrition	Kao's Sanitary Products Research Laboratories presented a paper titled, "Impacts of Carbohydrates with Different Insulin-Stimulating Effects on Postprandial Lipid Metabolism in Dogs" at the 3rd Academic Conference of the Japanese College of Veterinary Internal Medicine (Supported by the Ministry of Agriculture, Forestry and Fisheries, the Japan Veterinary Medical Association, and the Japanese Society of Veterinary Science), and received the Japanese Society of Pet Animal Nutrition's Best presentation Award in recognition of the significance of anti-obesity technology based on lower GI carbohydrates.
Kao Receives 3rd Intellectual Property Association of Japan Industrial Merit Award	Amid growing interest in intellectual property management - the application of patents, trademarks, and other intellectual property in business activities - Kao was presented with the 3rd Intellectual Property Association of Japan Industrial Merit Award. This award recognizes Kao's management focus on intellectual property and its outstanding achievements in the creation and application of intellectual property as a domestic corporate member of the association.
Kao Selected as Best Deal in the Domestic Bond Category of the 13th Deal of the Year Awards	In July 2006, Kao issued 100 billion yen in bonds to replace short-term financing used to acquire the shares and intellectual property rights of Kanebo Cosmetics. At the 13th Deal of the Year Awards, which were presented in recognition of outstanding financing skill, the financing activities undertaken by Kao were selected as the Best Deal in the domestic bond category.

# Responsibilities to Stakeholders

Responsibilities to Consumers and Corporate Customers  
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Responsibilities to Employees  
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Responsibilities to Suppliers  
**41**

Responsibilities to Shareholders and Investors  
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For Local Communities  
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Kao has implemented various systems for listening to and engaging in dialogue with consumers, and applies what it learns in product development and improvement, and the provision of information to consumers who have bought Kao products.

### Systems for Applying Consumers Voices in Yoki-Monozukuri

Kao aims to achieve its corporate mission of striving for wholehearted satisfaction and enrichment of the lives of people globally through *Yoki-Monozukuri* from the consumer's perspective. We do this based on our corporate philosophy, The Kao Way. To achieve this mission, we promote the incorporation of consumer voices in *Yoki-Monozukuri* throughout the company. We carefully listen to the voices of consumers, use our information systems to share throughout the company what we learn from communications with consumers, and apply this information in areas like product improvement and development of new products.

#### Kao ECHO System Information infrastructure supporting Yoki-Monozukuri

Kao's Consumer Communication Center, which listens directly to consumers, works with consumers to solve their problems by developing a deep understanding of the daily life characteristics behind their questions and engaging them in two-way communication. For us, consumers are more than just users of Kao products.

The Kao ECHO System is information infrastructure that provides rapid, accurate, and courteous service through our Consumer Communication Center.

The Kao ECHO System incorporates a database of a wide variety of information ranging from product data, to histories of ingredient changes, and daily life information related to products, for all Kao consumer products. The Kao ECHO System makes it possible to rapidly search for and identify necessary information, and respond to consumer inquiries.

Taking appropriate measures to protect personal information, the system accumulates each day's information on consumer inquiries in a database and makes it available for companywide browsing the next morning. We are using this system to examine data like inquiry trends by product and inquiry rates in terms of production volume, and are applying data in areas such as product development and marketing to constantly reflect consumer voices in *Yoki-Monozukuri*.

In fiscal year 2006, we received approximately 133,000 consumer inquiries, 10% more than in the previous year.

### Feeding back Consumer Voices into Products

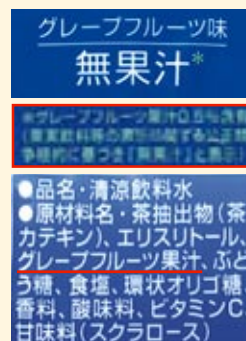
Through links among our development, research, production, and other relevant divisions, we use the opinions and requests that we receive through close communication with consumers as feedback for improving existing products and developing new ones. We apply what we learn from consumers not only in improving product performance but also for purposes like making containers easier to use, clarifying labels, and developing advertising messages.

#### TOPICS

#### An example of consumer voices resulting in a label improvement *Healthya Water*

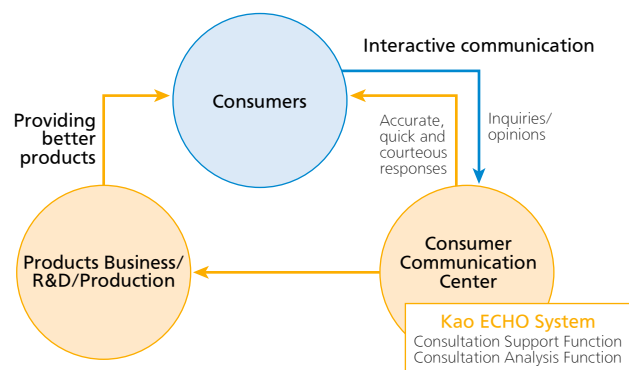
*Healthya Water* contains only a tiny amount of grapefruit juice (0.5%), but, in accordance with regulations, we had been labeling products with less than 5% fruit juice

content as containing "No Fruit Juice." However, we had received inquiries about grapefruit juice content from consumers who were taking antihypertensive drugs and refraining from drinking grapefruit juice, so, in August 2006, we added the words "Includes 0.5% grapefruit juice" to the *Healthya Water* label for the benefit of people who need this information.

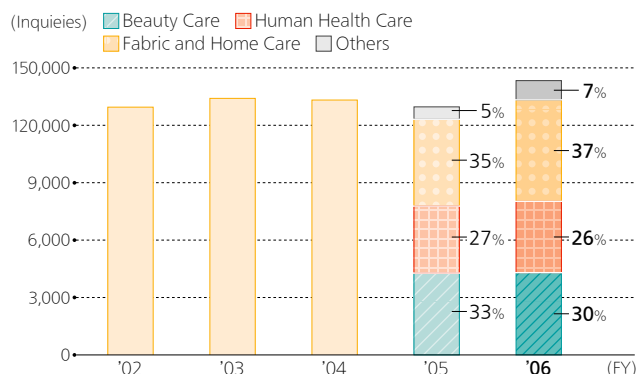


Revised label information

### Mechanism to Reflect Consumer Voices in Products



### Consumer Inquiries Trend (Data for Kao and Nivea Kao)





## Surveying Consumer Attitude and Consumer Satisfaction

To accurately gauge satisfaction with Kao products, our Consumer Communication Center regularly conducts attitude surveys among consumers and garners data face-to-face through means like focus groups and in-home surveys.

It also conducts annual surveys to measure satisfaction with our responses to consumer inquiries. In the survey for fiscal year 2006, over 90% of the people said that they were either “very satisfied” or “satisfied” with the response they received. Moving forward, Kao is aiming to further increase the quality of its communications and responses to consumer inquiries by benchmarking inquiry response satisfaction.

## Appropriate Information Provision

The information consumers need spans a broad range. Examples include information on proper ways to use products, safety and environmental information, and daily life information related to products. At Kao, we continuously develop products that respond in a timely way to consumer needs and provide various kinds of information based on years of research.

### Educational activities and information provision from the consumer's perspective

Kao's Consumer Communication Center holds seminars for consumers and experts under themes like “lifestyle-related diseases” and “food education” (See page 11). Additionally, for cases in which there have been many consumer inquiries, we provide information via channels like our website.

In fiscal year 2006, a rash of food poisoning cases due to norovirus led to an increase in inquiries regarding chlorine-based bleach, so we posted relevant information on our website in a Q&A format.

Concerning product labels, we pay careful attention to developing content and expressions that reflect changing consumer needs, so that our products can be used safely and appropriately.

### TOPICS

#### Participation in the International Association for Universal Design

In October 2006, Kao participated in the 2nd International Conference for Universal Design and introduced examples of pioneering universal design, which included



Kao's booth

putting notches on shampoo containers to help distinguish them from conditioners. And we also showed easy-to-open cosmetics boxes, easy-pour packages for shampoo refills, and other innovations.

### Provision of information to disabled people

Kao, in an effort to promote barrier-free societies, works with the Accessible Design Foundation of Japan to produce videos that encourage understanding of the lives of various types of disabled people and donates these videos to schools throughout the country, at their request. We also distribute for free audio CDs and Braille seals that make it easier for visually disabled people to comfortably use Kao products.

## Global Promotion of *Yoki-Monozukuri* from the Consumer's Perspective

The entire Kao Group is pursuing initiatives for incorporating consumer voices in *Yoki-Monozukuri* on a global basis.

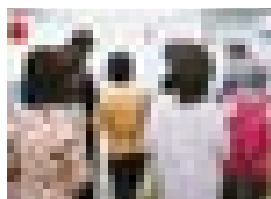
In September 2006, Kao held the second meeting for managers in charge of consumer communication in the Asian region. The meeting included participants from China, Hong Kong, Taiwan, Vietnam, Thailand, Indonesia, Malaysia, and Australia, and deepened their awareness of the company's stance on incorporating consumer voices in *Yoki-Monozukuri* via active reporting on their activities.



Participating managers from various countries

## Emphasizing Partnerships with Consumer and Other Organizations

In October 2006, Kao participated in Kurashi Festa 2006, a joint project of the Tokyo Metropolitan Government and consumer organizations. We took part in symposiums and events under the theme “environmentally friendly products and daily life.” We provided information on how we are helping to protect the environment with compact detergent products, described examples of how we have facilitated container recycling, and provided other information on what we do for the benefit of the environment.



Kao's booth

Kao aims to grow together with our corporate customers through exchanges of valuable information with various retail business partners and close collaboration with customer companies.

### Collaboration with Retailers

Kao provides its consumer products and cosmetics to consumers via retail business partners (supermarkets, drugstores, etc.) We sell our products to retailers through Kao Customer Marketing (Kao CMK), a company we formed in April 2007 through the merger of two sales companies, one specializing in household goods and the other, in cosmetics.

Kao CMK works together with Kao Merchandising Service (KMS), a company that supports retailing activities, to not only provide Kao products but also engage in exchanges of valuable information with retailers, for the benefit of mutual growth.

Therefore, in addition to normal sales and retailing support activities, Kao CMK and KMS also hold regular information exchange meetings with retailers. At these meetings, Kao provides product information to retailers who in turn give their opinions of product sales performance and consumer reactions. In fiscal year 2006, information exchange meetings were held with approximately 400 retailers throughout the country.

#### Provision of valuable information to retailers

Product information Seminars are an example of how Kao provides information to retailers. These seminars use the Product Education Centers located in Kao CMK branch offices to provide retail store personnel who deal with consumers directly with information on matters like product characteristics, product performance and use, and market trends. Through seminars like these, which aim to impart detailed knowledge of Kao products to retail personnel, we help to invigorate communication with consumers and improve the performance of retail stores. In fiscal year 2006, we held 1,034 Product information Seminars.

### Collaborative System between Kao CMK and Retailers

**Contributing to the success of retailers who are the interface between products and consumers**

#### Role of Product Education Centers

The Center holds country-wide seminars for retailers on how to give consumers the best advice, mainly for high value-added products, as providing appropriate information at the storefront is particularly important for these products.



#### Soliciting product ideas

Retailers' staff in charge of stores and Kao CMK's staff share storefront information (sales, store displays) provided by retailers, as an interface with consumers. The results are then passed on to the Product Development division.

**Incorporating retailer/consumer information into product development and improvement of sales activities**

### Collecting valuable information from retailers

Product Idea Collection Program are one example of how information gathered from retailers contributes to improvements in business activities. In 2006, we held our third program and received 2,774 submissions from 1,358 full-time, contract, and part-time employees at Kao CMK and KMS, which are in constant contact with retailers. These ideas are valuable information originating from retail sales locations and are referred to in product development. In addition, information gained from retail stores is provided as feedback to relevant Kao Group divisions when it is appropriate to do so. In fiscal year 2006, ideas on creating retail environments that provide clearer visual information for consumers and make it easier for them to purchase products led to the improvement of sales promotion tools and product packaging.

### TOPICS Social contributions via GCI\* Japan

As a result of endless improvement and human effort, consumer goods distribution in Japan incorporates one of the most sophisticated supply-chain systems in the world. However, adjustments to a broad array of operational and processing standards have caused the systems of production, distribution, and sales companies that support this to develop inefficiencies from the perspective of providing value to consumers.

GCI Japan (a voluntary organization composed of 88 private-sector companies as of April 2007) cooperates with standardization organizations active throughout the world to standardize data exchange items for product information, order entry and reception information etc. and promote the growth of Electronic commerce, which integrates production, distribution, and sales. The ultimate purpose of GCI Japan is to bring about an efficient, high-quality distribution system in Japan.

As one of its production, distribution, and sales industry development activities, Kao, as a managing member, has been promoting GCI Japan's activities since its founding in 2002 (At the time, GCI Japan was known as GCI Study Group GCI. It took on its current name on April 1, 2005.) Kao will continue with initiatives aimed at optimizing all three levels of the supply-chain — production, distribution, and sales — to provide value to consumers.

\*GCI Global Commerce Initiative

## Collaboration with Customers (Chemical Business)

Kao's chemical business, which is one of Kao's core businesses, provides chemical products (intermediate materials) to a broad range of customer industries throughout the world. This business is comprised of three operations: Oleochemicals (fats and oil derivatives), performance chemicals (surfactants), and specialty chemicals (information materials, fragrances). (See page 13)

All of these operations must pursue development consistent with rapidly changing market needs and must engage in detailed information exchanges with customer companies to offer safe, high-quality products. Kao not only provides product information and technical services, it also promotes product safety by preparing MSDSs in various languages and providing the latest information on matters like social responsibilities and regulatory developments relevant to chemical manufacturing. Additionally, we receive market news, information on user desires, and information on safety and other matters from customer companies, and engage in joint development with customer companies when necessary. Responding to the needs of customer companies focused on cutting their environmental burden, we are promoting environmentally friendly product development. (See page 13)

### Partnerships with dealers

In our chemical business, there are many products sold by dealers, whom we regard as business partners. Kao, therefore, maintains close communications with dealers through daily business meetings and information exchange sessions, and has built an extranet with dealers. We promote increases in operational efficiency by using an EDI (Electronic Data Interchange)-based ordering system.

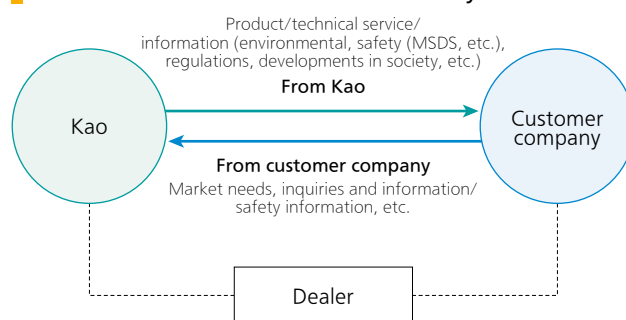
In information exchange sessions, we provide information to promote understanding of policies regarding Kao's business and Responsible Care (RC) activities, and mutually confirm progress on ISO acquisition, personal information management, and other basic RC matters. We also provide explanations of Kao's CSR approach and our Business Continuity Plan (BCP), and seek the understanding and cooperation of dealers. Furthermore, we share REACH, GHS, and other information on developments in chemical regulation throughout the world in an effort to foster a common understanding of the business environment for chemical product sales.

## Collaboration with Professional-use Product Customers

Kao's professional-use product business provides products and services integrating Kao's years of surface science and microorganism control technology to food service companies, hotels, hospitals, laundries, and other businesses and facilities with needs for advanced sanitation management. Kao Professional Services, a Group company, closely examines environments in which Kao products will be used and identifies the individual needs of customer companies. It provides products that deliver cleanliness and sanitation, information on topics like product management and use, and services.

For example, for hospitals and nursing-care facilities, Kao Professional Services not only provides hand cleansers, disinfectant, and other products, but also offers hospital infection prevention and other seminars for facility employees, and provides information on key points in sanitation management, correct product usage, and other topics. Regarding diversifying customer needs, it provides comprehensive solutions including improvement proposals, results validation, and manuals, all based on examinations of individual work environments. In doing so, it also provides total support for improvement of sanitary, safety and environmental management for the operations of customer companies.

### Chemical/Professional-use Product Sales System Overview



Aiming to create productive relationships that lead to both employee and organizational development, Kao is pursuing the creation of work environments and systems that develop the characteristics and capabilities of individuals.

### Human Capital Development and Training

Kao's basic approach to human capital development emphasizes simultaneous development for individual employees and the company. We reflect this approach in each type of human capital system and in activities undertaken to create our work environment and corporate culture. We aim to integrate the capabilities of individual employees into the overall capabilities of the company.

To give a specific example, we develop various types of training programs to fit individual jobs and roles, based on our training policies. We create courses that respect self-initiative and support opportunities for employees to study of their own volition.

#### Policies Regarding Human Capital Development (HCD) Training

To reinforce the human resources who will be necessary for the company's continuous development, Kao provides education that contributes to the growth of both the organization and individuals in a planned and comprehensive manner, based on a long-term perspective.

1. We provide high-quality educational opportunities for personnel with motivation and ability.  
For employees with motivation and ability, we provide comprehensive education of a high level and in a planned manner in order to nurture personnel who will be regarded as professionals.
2. We implement basic education in a timely manner as appropriate for the particular stage in each individual's career.  
The education implemented contains practical content in the form of knowledge and skills required for job performance, in accordance with an individual's role and the stage in his or her career.
3. We place importance on employees having an attitude of "Learning independently" and we support self-enlightenment.  
We provide many different programs for learning knowledge and skills in accordance with an individual's job and roles.

### Summary of Training Programs

	Business Intelligence (Corporate)		Professional Intelligence	Self-development
Management level	<b>Core Talent Programs</b> <ul style="list-style-type: none"> <li>Advanced Management Program</li> <li>Business Task Study</li> <li>Business Leader Training</li> <li>Next-generation leader development training</li> <li>Outside School</li> </ul>	Global Program	<b>Advance Course</b> <ul style="list-style-type: none"> <li>Outside School</li> <li>Cross Industrial Associations</li> <li>Professional Schools</li> </ul>	<b>Self-developed</b> <ul style="list-style-type: none"> <li>English</li> <li>PC Skills</li> <li>Business Skills</li> <li>Acquisition of Qualifications</li> <li>Corresponding Education</li> </ul>
Core Middle level	<b>Management Programs</b> <ul style="list-style-type: none"> <li>Training for newly promoted employees</li> <li>Human Resource Management</li> <li>Career Support for Middle Staff</li> </ul>			
Junior level	<b>Basic Business Knowledge &amp; Skills</b> <ul style="list-style-type: none"> <li>Before Joining Training</li> <li>After Joining Training</li> <li>Follow-up Training</li> <li>Step-up Training</li> </ul>	Promotion Task	<b>Basic Course</b> <ul style="list-style-type: none"> <li>Basic Technical Knowledge &amp; Skills</li> </ul>	

### Fair Evaluations and Compensation

Kao clearly states employee duties, roles, and responsibilities, fairly evaluates the capabilities and accomplishments of individuals, and reflects results in compensation and benefits.

To eliminate unfairness due to subjective evaluation standards, employee evaluations are adjusted within each division. Additionally, we are working to create a system that further enhances the objectiveness of evaluations by, for example, using Balanced Score Cards as evaluation sheets for employees at the level of manager or higher.

Furthermore, we provide training for evaluation, including People Management Training for employees evaluating subordinates for the first time, and companywide group training for employees recently promoted to manager.

#### Human resource evaluation system

Employees (subjects of evaluations) and their supervisors (evaluators) meet at the beginning of evaluation periods to discuss and determine work objectives for the employees during that period. Additionally, Kao has created systems for quantifying progress in achieving work objectives and objectively evaluating employees. Employees and supervisors meet again at the end of each period to evaluate achievements. We put substantial effort into increasing evaluation fairness and employee satisfaction with evaluations.

#### Initiatives to Pass on Technologies and Skills

Kao operates its Techno School, which provides selective training aimed at developing operating engineers, who will become core members of the Production and Engineering Division, and passing on to them technologies and skills.

The Techno School is long-term (seven-month) training targeting engineers in their 20s to 40s at each plant. Since the purpose of this training is to develop key employees of the Production and Engineering Division, it involves not only technical skill improvement in the form of hands-on training and the acquisition of qualifications but also lectures, sales training, and other programs for building character and broadening perspectives.

#### Employee Invention System

Kao introduced its Employee Invention System in fiscal year 2000. The intent of this system is to fairly evaluate the job-related inventions of employees, reflect accomplishments in compensation and benefits, and foster motivation for the future. Rewards are determined in accordance with the Compensation System for Employee Invention and through a fair and transparent process, which is disclosed to employees via an intranet.

## Promoting Diversity and Respecting the Individual

Kao's Business Conduct Guidelines require respect for employees' individual human rights and diversity, and maximization of their potential. This policy forbids discrimination based on culture, nationality, religion, creed, race, gender, age, physical handicap, and other factors and aims to build an equal partnership that respects the dignity and value of individual employees.

In that connection, we have been pursuing EPS\* Promotion Activities since 2000, with the aim of respecting diversity among individuals and creating a certain type of working environment — one that is discrimination-free, positive, and open, and lets employees approach their work with motivation.

In fiscal year 2006, we undertook initiatives in accordance with the Law for Measures to Support the Development of the Next-Generation.

\* EPS Equal Partnership

### Supporting the success of women

To allow employees to exercise their capabilities regardless of gender, Kao is working diligently to expand opportunities for women to work and succeed.

In fiscal year 2006, women accounted for 6.7 percent of Kao management positions, 0.7 percent more than in the prior fiscal year.

Moving forward, we'll continue to take measures that provide women with equal opportunities to exercise their capabilities and build their careers.

### Employee Data

		FY2004	FY2005	FY2006
Permanent employees	Female	3,131	3,022	9,123
	Male	8,316	8,289	9,744
Contract employees	Female	1,989	2,194	6,161
	Male	94	90	148
New employees (permanent employees + contract employees)	Female	791	798	2,199
	Male	145	168	307
Employees who took maternity leave	Female	134	142	355
	Male	1	1	32
Percentage of female executives (%)	* Data is based on Kao Corporation.	5.4	6	6.7
Changes in Employment Rate of Persons with Disabilities	* Data is based on Kao Corporation. As of June ended.	1.95	1.89	2.13

\* For fiscal years 2004 and 2005, employee data was gathered for employees of Kao, Kao Customer Marketing, Kao-Quaker, Kao Professional Service, and Ehime Sanitary Products. Beginning with fiscal year 2006, employee data also includes employees of Kanebo Cosmetics and Kanebo Cosmetics Sales.

### Work-life balance

Since the 1980s, Kao has been creating systems that permit employees to choose from a variety of flexible work styles, fostering the development of a corporate culture and building awareness that makes it easy to use these systems. We have also been actively pursuing other activities that support a healthy work-life balance.

Consistent with plans in April 2005, created in accordance with the Law for Measures to Support the Development of the Next-Generation. In fiscal year 2006, we implemented a new system, held a forum and photo contest, and published an employee guidebook. In the forum, we featured talks by outside speakers and examples of male employees of Kao and other companies who have taken paternity leave to encourage men to participate in child rearing. As a result of such efforts, Kao was recognized by the Tokyo Labour Bureau in April 2007 as a company that actively promotes policies for the development of the next generation.

Also in fiscal year 2006, all Kao female employees who gave birth took maternity leave, and 97% later returned to work. Twenty-six male employees took maternity leave. New systems introduced in fiscal year 2006 include the following:

- Flexible working hour system
- Extension of the staggered working hours (previously ended when the subject child became three years of age, now extended to the time when the subject child enters primary school)
- Payment of salary and benefits for the first five days of maternity leave
- Payment of 100 percent of salary when employees have difficulty meeting daily expenses during maternity and child rearing or nursing care leave.



Work-Life Balance Guidebook



Next-Generation Forum



Mark designating companies certified under the Law for Measures to Support the Development of the Next-Generation



### Promoting the employment of disabled people

Under its policy of supporting “the independence of disabled persons as members of society to create a society where all people with and without disabilities work and live together,” Kao promotes the employment of disabled people. Kao Peony, a special subsidiary that provides a workplace for people with intellectual disabilities, exceeded its performance goals for its initial year of full-scale operations, which began in April 2006.

As of June 2006, Kao’s employment rate for disabled people was 1.89%, or 2.13% when the special subsidiary is included. Moving forward, Kao will continue to actively promote the employment of disabled people.

### Introduction of the Senior Partner System for re-employing retirees

As the working population has declined with the falling birthrate, securing a stable workforce and transferring the mature business skills and expertise of experienced workers have become matters of great importance for companies.

In April 2006, therefore, Kao introduced its Senior Partner System for reemploying, on a contract basis, retirees who possess advance knowledge, business skills or technical know-how, and a desire to work. Under the present system, those eligible for reemployment are limited to people who will perform special assignments requiring expert knowledge. There are, however, plans to expand the range of eligible people in April 2008.

### Creating a workplace free of discrimination and harassment

At Kao, employees undergo training on human rights and the prevention of harassment when they are newly hired or promoted.

This training, which is led by both EPS and compliance promoters, reinforces the provisions of Kao’s Business Conduct Guidelines and promotes understanding of equal partnership.

Additionally, we have established compliance hotlines inside and outside the company and respond to questions

and reports received by telephone, fax, e-mail, and letter. We pursue activities to fight discrimination and harassment from multiple other perspectives, as well.

## Reflecting the Voices of Employees

### The FIND employee opinion survey

Since fiscal year 2001, Kao has been conducting the FIND employee opinion survey every other year, and disclosing results to employees via an intranet. Additionally, so that results lead to improvements in operational processes and higher productivity, each division creates an action plan and implements it.

Efforts are made to link action plans to practical, ongoing organizational activation measures by, for example, applying action plan implementation results to employee evaluations.

In fiscal year 2006, action plans created based on fiscal year 2005 survey results were implemented.

We intend to introduce this process to overseas companies, as well, beginning in fiscal year 2007.

### Emphasizing the importance of dialogue with employees

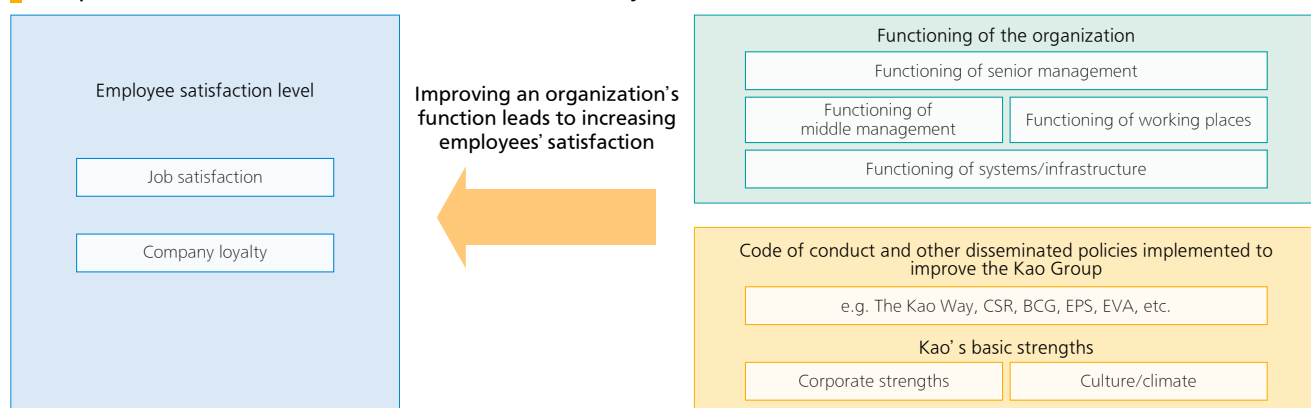
Kao holds Management-Employee Meetings to foster communication between top management and employees. At these meetings, in which 20 employee representatives of all Kao facilities participate, the President explains the company’s current status and future strategies, and answers questions. In fiscal year 2006, two of these meetings were held.

Additionally, each individual Kao facility holds labor-management meetings, operates Employees’ Welfare Committees, and engages in other such activities, actively pursuing mutual understanding between employees and management. Committee



Management-Employee Meetings

### Composition of Questionnaire Items for “FIND” Survey



meetings held at individual Kao facilities also perform the important role of reporting Management-Employee Meetings results. These activities will be continued in pursuit of further organizational invigoration.

Overseas, the Kao European Works Council was established in 1996. Employee representatives from Kao's European affiliates participate in an annual meeting at which persons responsible for European businesses explain the current situations and future plans of those businesses, and discuss various matters. The May 2006 meeting was held in Spain.

## Consideration for the health and livelihoods of employees

### Health management support

Kao, aiming to promote health consciousness among employees and help more employees maintain their physical and mental health, began its Kao Health 2010 health program in fiscal year 2005. Health guidance focused on the prevention of lifestyle-related diseases is provided based on the results of employee health examinations and interviews. Also, various support activities intended to help employees make voluntary changes to address lifestyle-related diseases are performed in cooperation with the health insurance mutual association.

### Mental health care

Kao is making a significant effort to provide mental health care, so all employees can be healthy in mind and body.

Our in-house health counseling room accepts consultations by telephone, e-mail, and personal interviews.

Additionally, as an employee support program, we work with specialized outside organizations to provide telephone counseling and e-mail-based-counseling guaranteeing a response within 24 hours for Kao Group employees. Face-to-face counseling is also offered.

### Preventing overwork

In the wake of legal revisions and changes in working conditions, Kao introduced its Work Management System in April 2005 to help manage work from the perspective of human risk management.

The purpose of the system is to prevent excessive work through such measures as the prevention of unpaid overtime, compliance with regulations regarding maximum working time, and the prevention of health problems resulting from long working hours.

Under this system, the hours worked by individual employees are checked once a month by the employee and his/her manager. If statutory limits are exceeded, a Special Extension Notification must be submitted. No more than two of these notifications may be submitted per year. In addition, if overtime exceeds 100 hours per month, or 80 hours per month on average over a two to six month period, working hour controls are tightened by, for example, having the subject worker attend a health interview each time the limit is exceeded. All of these measures are taken in an effort to prevent excessive work.

### Support for retirees

To support employees after retirement, Kao holds Life Plan Seminars for all employees when they turn 55.

These seminars take place over two days and one night for those who want to participate. They include explanations of Kao's pension system and the national social insurance system, presentations by outside speakers who perform simulations of life on a pension and provide guidance and advice on post-retirement life, and other information. Between 1992, when the seminars were inaugurated, and the end of March 2007, participants numbered 1,270.

With the transition from retirement allowances to company pensions, Kao adopted both a defined benefit (Cash Balance) and defined contribution pension plan, which employees may freely choose to manage their pensions.

## Participation Rate of FY 2006 Annual Health Checkup

- Participation rate of checkup: 99.9%
- Follow-up rate\*: 82.7%

\* Percentage of employees who received health guidance among those who took health checks.

## Achievements of Activities to Address Life-Style Improvements in FY 2006

- Challenge Walking (to encourage the adoption of exercise as a part of daily life)
- Support to stop smoking at medical facilities (support to stop smoking)
- Kenkou Tatsujin Program (support to weight loss)
- Other: Assistance for health-promotion activities at individual Kao facilities, etc.

## Occupational Safety

### 2006 Disasters and Accidents, and Kao's Response

#### Occupational accidents in the Production & Engineering and Research & Development Divisions

In 2006, the Production & Engineering and Research & Development Divisions had one employee who suffered an injury resulting in lost work days, the same number as in 2005. This accident was a fall at a facility exit resulting in a broken leg. In total, 21 employees suffered accidents during the year, three less than in the previous year. In terms of trends, the number of occupational accidents associated with equipment and facilities has declined, while the number of ordinary accidents, like falls or tripping on stairways or floors, and the number of accidents from contact with toxic substances or hot surfaces during work are heading upward.

Moving forward, the Research & Development Division, which performs test operations and other nonstandard work, will carry out risk assessment and residual risk education, which is already being carried out by the Production & Engineering Division. We will also reemphasize work procedure and other reviews, and compliance with rules like those requiring the use of safety devices.

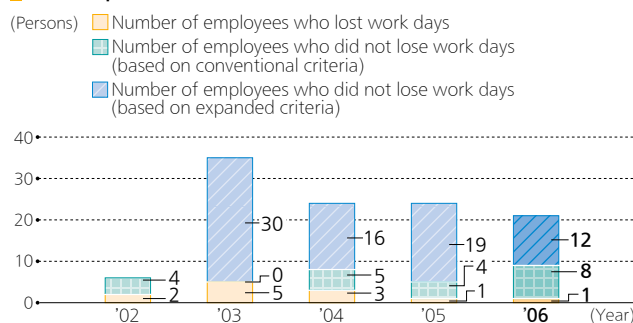
#### Occupational accidents throughout the Kao Group in Japan

At Kao Group companies and affiliates there were a total of 114 occupational accidents in 2006, 32 of which resulted in lost work days. These figures compare to 106 and 30, respectively, for 2005. Increases, therefore, occurred at both levels.

When accidents occur at affiliates or divisions, reports are shared to prevent occurrences of similar accidents and the information is used in training. As a result of risk assessment and the development of preventive measures, the number of accidents occurred during work procedures or in connection with facilities declined from the previous year.

On the other hand, an increase in accidents that could happen in daily life (e.g.: being hit by another vehicle during sales activities, tripping, missteps, etc.) was the primary cause for an increase in the total number of occupational accidents.

### Changes in the Number of occupational Accidents in the Production & Engineering and the Research & Development Divisions



Looking to the future, we will continue safety activities and focus on improvements that will allow us to reduce the number of these accidents, as well.

#### Plant fire

Since the methanol tank explosion at a plant in Malaysia in February 2006, the Kao Group has experienced no serious accidents, but, in 2006, there were several small fires at plants and other facilities both in Japan and abroad.

Kao takes these accidents very seriously, and its Production & Engineering Division has led the way in revising construction protocols and various procedures, taking other measures to prevent recurrences, and implementing facility-based measures to prevent fires. It has also enhanced patrols, maintenance, and other activities to prevent the ignition of fires by substances that leak during production and by worn-out equipment, and taken steps like performing safety assessments of chemical facilities.

In 2007, we will determine the implementation status of these actions and what results have been achieved through an internal audit.

### Emergency reporting training

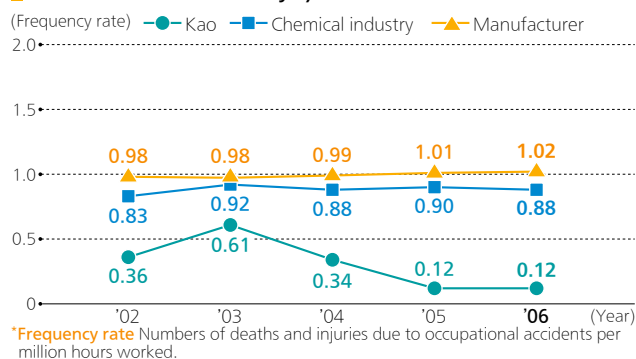
In November 2006, Kao held a companywide training exercise for emergency reporting in the wake of 3 supposed major earthquakes: the Tokai, Tonankai, and Nankai earthquakes. This exercise focused on emergency communications among the six Regional Countermeasure Offices (including a new center for Kanebo Cosmetics), the 18 Local Countermeasure Offices (covering 31 workplaces), and the Secretariat of Disaster Response Headquarters established in the Kayabacho Office.

Additionally, the Kayabacho and Sumida Offices performed a drill in which employees walked back home as they might in the event of a disaster.

### Asbestos control measures

Control measures for asbestos used in the building have been completed. Pipe-sealing containing asbestos posing no airborne risk in the factories will be replaced according to plans submitted to the Japan Chemical Industry Association. Replacement work is scheduled for completion by 2008.

### Changes in occupational Accident Occurrence (frequency rate of accidents with more than one lost day\*)



Kao is strengthening its partnerships with suppliers according to these three fundamentals: Fairness, compliance/ethics, and social responsibility.

### Collaboration with Suppliers

#### Systems for cooperating with suppliers

Raw material, packaging & container material, equipment, and other suppliers are indispensable partners in pursuing our business activities. Kao pursues procurement activities in accordance with its Guidelines for Procurement of Raw Materials and based on the following three fundamentals: Fairness, compliance/ethics, and social responsibility. We work to strengthen partnerships by, for example, sharing our business purposes with our suppliers and exchanging technical information required for raw materials of the quality and specifications we demand.

#### Meetings with suppliers

Kao is striving to deepen mutual trust with suppliers through communications in daily business transactions with each company and by creating opportunities for regularly exchanging information and opinions.

In fiscal year 2006, we held a meeting with suppliers under the theme, "Request for Cooperation with our CSR Procurement" and welcomed participation from 194 companies providing us with raw materials, packaging materials, equipment, and other items.

#### Guidelines for Procurement of Raw Materials

Kao will conduct fair purchasing activities based on compliance and ethics. Kao will make efforts to assume corporate social responsibility, giving due consideration to enrichment and safety in its purchasing activities.

##### 1. Fairness

- (1) Kao selects suppliers based on rational judgment on the quality, price, and the delivery lead time of raw materials, as well as the stability of business management, manufacture/provision capabilities, commitments to environmental conservation.
- (2) Kao provides suppliers with an opportunity for fair competition, without regard to nationality.

##### 2. Compliance/ethics

- (1) Kao shall observe both letter and spirit of all applicable laws and regulations.
- (2) Kao will not disclose any confidential information acquired about suppliers through its procurement transactions. Kao will not conduct procurement transactions that infringe the intellectual property rights of third parties.
- (3) Kao will not conduct reciprocal trade for the purpose of selling Kao's products/services.
- (4) Kao shall keep the receiving and giving of business gifts and entertainment within bounds that are recognized as acceptable business practice and internal regulations should be observed. In principle, individuals responsible for procurement transactions are not allowed to be entertained by suppliers, or give and receive gifts.

##### 3. Social responsibility

- (1) Kao aims to contribute to "the achievement of a sustainable society," gives due consideration to resource protection and environmental conservation, safety, and human rights, as well as making efforts to assume corporate social responsibility.
- (2) Kao shall exchange necessary information with suppliers, and mutually evaluate the quality and prices of the materials, services, and each other's businesses and shall engage in good faith mutual evaluation with our suppliers in order to continue to raise the level of quality of our respective businesses.

#### Quality-improvement meetings

For items with quality issues, we held quality-improvement meetings with suppliers, determined mutually agreeable improvement measures in pursuing raw material quality-improvement activities.

In fiscal year 2006, we held 99 quality-improvement meetings with 46 companies to address issues like malformed and poorly printed packaging materials and containers.

#### Supplier Satisfaction Survey

Kao has an outside institution conduct our Supplier Satisfaction Survey once every two or three years to determine whether our suppliers think we are pursuing fair procurement activities that are within the law and ethical. The survey, which is anonymous, asks approximately 160 of our principal suppliers to rate us on approximately 30 items, like supplier selection, quality, price negotiation, supplier relations, ordering, and communications. The results are indexed and we reflect them in our procurement activities.

The next supplier satisfaction survey is scheduled in fiscal year 2007.

#### Examination of CSR procurement standards

##### *Stepping up from Green procurement to CSR procurement*

Kao, in order to promote green procurement, has evaluated both its primary suppliers and new suppliers for their building and use of Environmental Management Systems (See page 55) In fiscal year 2006, we also established our CSR Procurement Standards, which augmented our existing green procurement standards with items addressing social concerns. We are now examining whether our domestic and overseas suppliers meet these standards.

This examination, which began with a preliminary study, got underway in full in January 2007 and includes questions on 16 matters, including the 10 principles contained in the UN's Global Compact. These questions are being put to our principal suppliers. Those suppliers who do not meet our standards will be requested to create new systems that will allow them to do so and take other measures in furthering CSR procurement. In fiscal year 2006, we completed examinations of 377 principal suppliers in Japan and abroad.

##### *Participating in RSPO to further CSR procurement*

To further CSR procurement, Kao became a formal member of the RSPO (Roundtable on Sustainable Palm Oil) in April 2007. (See page 15)

Kao is pursuing information disclosure and other communication activities with the aim of gaining the trust of shareholders, investors, and society as a whole.

### Returns to Shareholders

#### Dividend policy and performance

Kao has set basic policies on internal reserves and distributions of earnings with the purpose of achieving profitable growth and stable performance. Regarding dividends, we emphasize stability and continuity and in fiscal year 2006 established the objective of meeting a consolidated dividend payout rate\* of 40%.

We regard the acquisition of treasury shares as a method for boosting long-term returns to shareholders and will flexibly consider treasury share acquisitions, while also considering capital expenditures, corporate acquisitions, other growth-related capital demands, and the need to increase capital efficiency.

Based on such policies, we decided to increase the annual dividend for the fiscal year ending in March 2007 by 2 yen per share, to 52 yen per share, marking our 17th consecutive annual dividend increase. The dividend payout rate came to 40.2%.

#### \*Dividend payout rate

The dividend payout rate is the percent of net income paid out as dividends.

### Information Disclosure and Communication

It is important to Kao to have the trust and respect of society, and it has established basic policies requiring timely, appropriate, and fair information disclosure to shareholders, investors, and all other stakeholders.

More specifically, we comply with the Corporation Law, the Securities and Exchange Law, various regulations, and rules set forth by the Tokyo Stock Exchange, in accordance with the Disclosure Guidelines we established in May 2006, and practice swift, fair disclosure of information covered by the Timely Disclosure Regulation. We also actively disclose Kao Group information that is valuable to society.

Moving forward, we plan to consider policies for strengthening communication with individual investors, which we believe is very important.

**HP** Investor information  
<http://www.kao.co.jp/en/ir/>

#### Invigorating the Annual General Meeting of Shareholders and improving the voting process

To provide shareholders with enough time to examine agenda items, Kao usually sends a convocation notice approximately one month prior to the Annual General Meeting of Shareholders.

In addition, to increase the number of shareholders who vote, we began employing an electronic voting method with the 2006 regular Annual General Meeting.

For the benefit of rapid, fair information disclosure to the foreign shareholders who hold approximately half of our shares, we simultaneously prepare and send English and Japanese convocation notices, and post background information and voting results from the Annual General Meeting of Shareholders in both English and Japanese on our website.

The 2006 Annual General Meeting was attended by 725 shareholders who, with opinions and questions on a wide range of topics like the appointment of female executives,



Annual General Meeting of Shareholders

consumer-oriented product development, human capital development policies, and policy regarding investment units, made for a lively meeting.

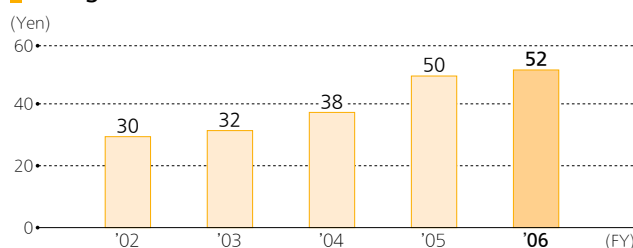
#### IR activities

Through the shareholder and investor briefings given below, as well as coverage by news media and other channels, Kao diligently works to swiftly and accurately report on its performance and financial situation.

Furthermore, our top management proactively participates in dialogues with shareholders and investors on occasions such as financial results briefings and meetings held by investment securities firms, in support of our overall efforts to promote smooth two-way communications.

In fiscal year 2006, we enhanced our systems for directly communicating views of shareholders and investors, which we gain through daily activities, to management, and used this information to improve our IR activities.

#### Changes in Dividends Per Share



#### Overview of IR Activities

- Financial results briefings: Held twice a year (same day as results announcement)
- Overseas IR tour: Each held once a year (North America, Europe)
- Business briefing: Held once a year
- Individual interviews: Over 250 interviews in Japan and abroad
- Small meetings
- Overseas conference calls
- Information disclosure on website



Kao undertakes social contribution activities under the theme of “Nurturing the Next Generation,” provides assistance to those affected by disasters through its sales net work, and pursues other means of supporting local communities that are unique to Kao.

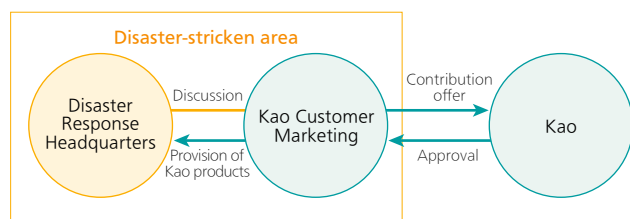
## Disaster Relief Activities

Kao’s Business Conduct Guidelines (See page 21) include requirements for suitable donations considering social standards, public interest and usefulness.

Regarding disaster relief, our policy is, in principle, to make the provision of assistance our top priority when a disaster occurs in Japan or any other country in which the Kao Group has operations.

For disasters that occur in Japan, we basically respond by providing Kao products. More specifically, once government establishes a disaster response headquarters, the closest Kao Customer Marketing unit, acting as a liaison, discusses needs with the headquarters organization and arranges the rapid donation of Kao products. These include mainly soap, toothpaste, and other personal care products, but also may include disposable diapers, sanitary napkins, and other products, depending on demographic factors. We do our best to donate those products for which there is the greatest need.

### Flow for Donating Disaster Relief Goods



### TOPICS

#### Relief to heavy rainfall disaster in July 2006

In response to heavy rains that damaged parts of Kyushu, the Sanin Region, Nagano Prefecture, and other areas of Japan in July 2006, Kao, with Kao Customer Marketing (formerly Kao Hanbai) fulfilling the role of liaison with disaster response headquarters in Nagano and Kagoshima Prefectures, provided detergent, disposable diapers and other products.

Additionally, as a first-of-its-kind trial in Japan, “Uru-Uru Packages” were provided to disaster-stricken households. This activity was planned by Nippon Keidanren, disaster-response NPOs, and other organizations, and Kao and other companies provided towels, masks, soap, and other products that would be useful when volunteers visited households. Kao specifically contributed soap and Nivea hand cream.



Uru-Uru Package

## Corporate Citizenship Activities

Since fiscal year 2000, Kao has been engaged in various social contribution activities under the unified theme of “Nurturing the Next Generation,” based on the characteristics of our businesses and social challenges we face today.

In fiscal year 2006, we continued to pursue Corporate Citizenship Activities that are unique to Kao. These activities were based on the results of external evaluations of our fiscal year 2005 Corporate Citizenship Activities, and we even worked to expand them. In that connection, we inaugurated the support “Creating Forests for Everyone” Project for the participation of university students on the occasion of the fifth anniversary of the Kao Creating Forests for Everyone environmental conservation activity. (See page 44)

### Kao’s Guidelines for Community and Cultural Activities

1. Conduct activities that play a role in nurturing the next generation.
2. Conduct activities aimed at contributing to the development of regional communities and culture.
3. Conduct activities that protect and nurture the environment to promote a sustainable society.
4. Conduct activities that promote a barrier-free society as a form of social support.
5. Conduct activities that make effective use of Kao’s resources.
6. Create an atmosphere in which every employee can participate in community activities as a good citizen.

### Areas of Social Contribution



### TOPICS

#### Activities of the Kao Foundation for Arts and Sciences

The Kao Foundation for Arts and Sciences supports fine arts, music, and other artistic and cultural activities, and original, basic scientific and technology research. It also engages in activities like providing assistance for, and sponsoring symposiums for comprehensive research that integrates the social and natural sciences.

In fiscal year 2006, we sponsored a symposium under the theme of “Faces and Culture” coordinated by Hiroshi Harashima, Professor at the University of Tokyo and the Chairperson of the Japanese Academy of Facial Studies.



Symposium

## TOPICS

## Activities of the Support “Creating Forests for Everyone” Project

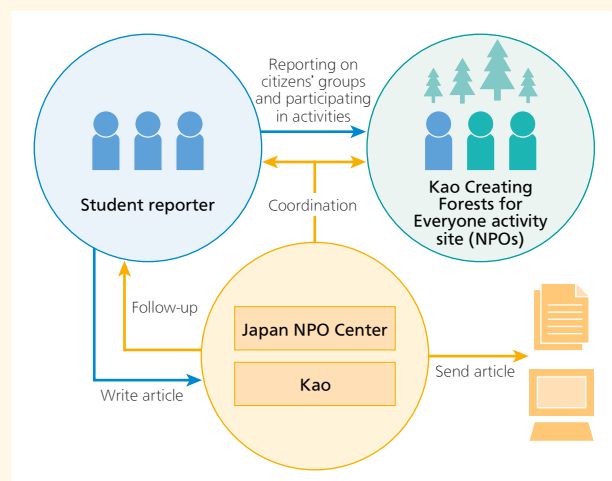
Kao has been supporting the Kao Creating Forests for Everyone environmental conservation activity being promoted by the Urban Green Space Development Foundation since 2000. The purpose of this activity is to promote the creation of green environments in places close to where people live, and it provides financial support for citizens' groups working to do that. In fiscal year 2005, Kao marked the fifth anniversary of Kao Creating Forests for Everyone by inaugurating Startup Grants to widen the scope of Kao's support, adding green-space-creation organizations that are just kicking off such activities or those that started less than one year ago. By March 2006, Kao had contributed a total of 140 million yen to 210 organizations.

In fiscal year 2006, we also launched the Support “Creating Forests for Everyone” Project, which will create a new circle of exchange by having university students with a keen interest in environmental conservation report on those activities. We did this after noticing that Kao Creating Forests for Everyone promoted not only environmental conservation but also intergenerational communication, helping to deepen mutual understanding. University students participating in the Support “Creating Forests for Everyone” Project, listen to people involved in green-space-creation activities, record their reactions to each perspective, and present their findings. This has deepened understanding of these activities and has given those pursuing them an objective take on how society views and assesses their activities. As such, the Support “Creating Forests for Everyone” Project, has become a productive opportunity for intergenerational exchange.

## ①Project launch

In 2005, we began evaluating Kao's corporate citizenship activities through an external evaluation organization. The results of those evaluations told us that Kao Creating Forests for Everyone was promoting not only environmental conservation but also communication among people of different generations, community-building, and community revitalization. We then launched the Support “Creating Forests for Everyone” Project, a

## Overview of the Support “Creating Forests for Everyone” Project



project in which university students report on the green-space-creation activities of citizens' groups, as a two-way platform for communicating the multidimensional significance of Kao Creating Forests for Everyone to society at large, and also as an activity in which communication itself becomes an activity for broadening exchange.

## ②Orientation

At the start of the project, in April 2006, students with an interest in environmental activities were publicly recruited to be Student Reporters. An orientation session was then held at the Kao Kasumigaura Training Center in June. There, Student Reporters were provided with necessary knowledge and information, organized into reporting teams, and encouraged to get to know one another.



Orientation

## Orientation Content

- Overview of Kao
- Kao's Environmental Activities
- Kao's Corporate Citizenship Activities and Kao Creating Forests for Everyone
- Reporting Team Workshop
- Citizen Activities
- Forest Creation Policies and Initiatives
- Reporting Techniques and How to Write Articles

## ③Student Reporters' Articles on Their Experiences

Between September and November, eight Student Reporters split up into teams of three and participated in nine citizen group activities two times each, gathering information as they did so. The roles of coordination, information recording, and information gathering were divided among team members.

## Citizen Groups Covered by Student Reporters

- Green Trust Utsunomiya Working Group (Utsunomiya City, Tochigi Prefecture)
- Teganuma Trust (Abiko City, Chiba Prefecture)
- Shiroy Environmental School, Specified NPO (Shiroy City, Chiba Prefecture)
- Forest Creation in 22nd Century, Jindai (Koganei City, Tokyo)
- Tama Green Volunteer Sinbokukai (Tama City, Tokyo)
- Asao Tama Beautiful Forest Society (Kawasaki City, Kanagawa Prefecture)
- Friends of Iwaya Green Space (Toyohashi City, Aichi Prefecture)
- Nurturing Society of the Seaside Forest (Hannan, Osaka)
- Sakuramamori Society (Takarazuka City, Hyogo Prefecture)



Fact gathering activities



Experiencing forest creation activities

#### ④ Report Preparation and Release

After they covered the assigned citizen group activities, the students prepared and issued reports. In the process, they confirmed information with citizen groups, had multiple meetings with people overseeing the website where their reports would be posted and the NPO Hiroba database, and eventually posted their reports on the Internet.



NPO Hiroba homepage

**HP** NPO Hiroba (only available in Japanese)  
<http://www.npo-hiroba.or.jp/>

#### ⑤ Report Meeting

In February 2007, the Student Reporters, orientation instructors, people representing the citizen groups covered, and others gathered at Kao's Kayabacho Office for the Report Meeting.



Report meeting

There, Student Reporters gave presentations on what they learned and discovered through the content covered in their reports and their experiences.

#### Comments of Student Reporters at the Report Meeting

- I gained a new sense that community ties are being created through forest creation activities. This was the first time for me to write a report on something I had covered, so I was a bit confused in the beginning, but I rewrote my report several times to be able to tell as many people as possible how wonderful these activities are.
- For me, the posting of something I worked very hard to write on the Internet was a very profound experience. I also felt energized and hopeful after meeting with people who are vigorously pursuing second lives after retirement.
- I think that the exposure of my report to a wide audience will permit not only me but also the members of the citizens' groups I covered to see the significance of their activities from a different perspective. Having that in mind, I thought that I had to be very careful to write a responsible report, and I put tremendous effort into doing that. Now that it's done, I'm satisfied with it and relieved that the members of the citizens' groups I covered are pleased with it.



Student Reporters

### Message



***Intergenerational communication through forest creation activities is revealing a new face of social contribution.***

**Natsuko Hagiwara**  
Japan NPO Center Managing Director

The Support "Creating Forests for Everyone" Project has two purposes. One is to widen the circle of support for citizen groups pursuing forest creation activities by communicating the significance of these activities to society at large. The second is to deepen understanding and knowledge by having students participate in and report on forest creation activities. We at the Japan NPO Center shared Kao's ideas and concepts in this regard and were privileged to cooperate in their realization. Specifically, we assisted with the recruitment of Student Reporters and coordination of scheduling with the groups to be covered, and helped to provide guidance and advice for

report preparation.

At the completion of this project, which took place over approximately six months, I was left with the feeling that this initiative was extremely significant in terms of revealing a new face of social contribution. The Kao Creating Forests for Everyone activity supports citizens' groups working to create forests, but the Support "Creating Forests for Everyone" Project, by providing opportunities for new dialogue between citizens' groups and students, allowed both to make discoveries and learn from each other. I believe that the resulting empowerment — the birth of new activity and communication from an increase in the number of people who have experienced intergenerational communication and understand its significance — is the greatest result of this initiative.

I am looking forward to seeing communication among students, citizens' groups, companies, NPOs, and others expand throughout society via this project.

## Exchanges with Individual Communities and Companies

Kao is actively pursuing various activities to promote coexistence with local communities and build a sustainable society. Our aim is to earn trust by making contributions as a good corporate citizen in the communities of our Japanese plants and offices, as well as overseas locations where we engage in business activities. Our activities are wide-ranging and may include plant tours, participation or cooperation in local events, cooperation with local business groups, community-building efforts, science education, family concerts, area clean-up efforts, or other activities depending on the characteristics of each community and the business activities of our facilities.

### Plant tours and science experiment classes

Kao offers tours at all of its Japanese plants. In fiscal year 2006, approximately 30,000 people, including local residents; primary, junior high, high school, and university students; and members of citizens' groups, visited our plants.

At our Wakayama, Kashima, Kawasaki, Tochigi, and Sakata Plants we host science experiment classes with an eye toward educating the next generation. To encourage children to take an interest in chemistry, we perform chemistry experiments and other activities using familiar Kao products and surfactants.



Toyohashi Plant



Sakata Plant

### Opening of the Kao Museum

Following a major renovation of the Sumida Office's small museum devoted to cleanliness in daily life, we opened the



Kao History Zone



Culture of Cleanliness History Zone

Kao Museum in January 2007. The Kao Museum has on display numerous historical materials Kao has assembled throughout its history of intimate involvement in efforts to improve cleanliness in daily life, and has devised ways to clearly depict developments in the culture of cleanliness. Together with exhibits, it also includes messages from Kao's founders, information on the history of our company, and displays of the latest Kao products born of *Yoki-Monozukuri*.

### Science education support

In support of high school science education, we hold science experiment classes led by Kao researchers. In fiscal year 2006, we held these classes at five high schools in Wakayama, Saitama, and other locations.

At our Wakayama Plant, we invited about 80 students and teachers from Toin High School to participate in a plant tour and performed science experiments using chemical products.

#### Science Classes Held in FY 2006

- Toin High School, Wakayama Prefecture
- Hiroshima Prefectural Fukuyama High School
- Soma High School, Fukushima Prefecture
- Omiya Musashino High School, Saitama Prefecture (Science Partnership Program)
- Saitama Prefecture Association of Physics and Chemistry Education in High School, Chemistry Sub Committee

### Kao Family Concerts

Kao sponsors concerts to give people living near our facilities an opportunity to hear live music and nurture their appreciation for music and art. These concerts are programs that function as contributions to local areas, and support for cultural enjoyment and local communities. They are held and managed by our employees who set up venues, make announcements, and perform other necessary tasks.

In fiscal year 2006, we held concerts at our Sakata and Tochigi Plants. The event at our Tochigi Plant was the first held there and featured a performance by an internationally famed violinist, Narimichi Kawabata. Attending the concert were 850 local junior high school brass band teams and teachers, and local residents, from whom an overwhelmingly positive response was received.



Family Concert (Tochigi Plant)



## Kanebo Cosmetics initiatives

### Medical Soin Esthetic

Kanebo Cosmetics is performing R&D on Medical Soin Esthetic (MSE) therapy for skin grafts performed in plastic surgery.

So that society can benefit from these results, headquarters staff of the Aesthetic Life Laboratory and the Beauty Research Institute have been performing this therapy once a month at the Department of Plastic and Reconstructive Surgery of Kitasato University Hospital since 1981.

The purpose of MSE is to aid recovery after surgery to remove birthmarks or improve the appearance of burns and scars created by accidents. Staff members perform esthetic therapy for outpatients, using combinations of massage and medical devices, which differ depending on symptoms. They also employ know-how unique to a cosmetics manufacturer to provide advice on how to use makeup to cover affected areas and highlight individuality. They also offer guidance on



MSE Therapy

skincare practices patients can perform themselves. In performing therapy, staff members do their best to understand patients and build relationships on trust.

## Kao Brands initiatives

Kao Brands Company views its responsibility for helping consumers and employees as extremely important, but there is also significant importance in building a strong relationship with the surrounding communities.

This is demonstrated by Kao Brands Company in various ways, such as supporting the United Way, the American Cancer Society and the March of Dimes. The United Way is a leading nonprofit organization developed specially for helping communities to succeed. The American Cancer Society is a community based organization dedicated to eliminating cancer through research and education. The March of Dimes supports the latest research on birth defects and educates the general public on how to reduce the chance of birth defects. But these are not the only ways that Kao Brands shows their motivation to help society.

A special way that Kao Brands Company's employees show their concern for helping the local community is by their volunteer work with the St. Bernard Mentoring Program. Twenty-three Kao Brands Company employees participate in the St. Bernard Mentoring Program called H.O.S.T.S. or Helping One Student to Succeed. Mentors meet with students once a week for 30 minutes and assist with teaching first, second and third grade students to read.

Although, six companies work with St. Bernard's Mentoring Program, Kao Brands Company has the highest number of participating mentors. These mentors are making a significant difference in the children's reading capabilities. At completion

of the program, students who were previously reading below their grade level had achieved or exceeded the requirements.

Kao Brands Company has been involved in this community



Employees participating as volunteers

program for three years and plans to continue exceeding expectations and building enduring relationships with the local community.

## Kao Corporation Shanghai initiatives

In the Minhang area of Shanghai, China, where Kao Corporation Shanghai's plant is located, a learning event under the theme of "beauty and pride of the local community" is held in July of every year with the financial backing of the local government. The purpose of this event is to help nurture children who can contribute to the future development of their community. Kao Corporation Shanghai, as a company with deep roots in the local community, has, since first being requested by the local government in fiscal year 2003, annually invited approximately 150 students from Maqiao Qiangshu School (primary and junior high school) to its facilities to hear explanations of what Kao Corporation Shanghai does and to participate in experiential learning exercises.

Explanations of what Kao Corporation Shanghai does include a video-based introduction to the business activities, products, and production activities of the Kao Group and Kao Corporation Shanghai; descriptions of product quality, environmental, and safety initiatives; and a plant tour. These activities are administered by the Human Capital and General Affairs Group, with the cooperation of the Plant Quality Assurance Division. In experiential learning exercises, students perform experiments using water-absorbing polymers, cleaning tests using Attack, and other such activities. The students who participate are enthusiastic and perform the experiments with great interest. These experiential learning events have been well received by not only students but also teachers and representatives of the local government. They are now in their fourth year and requests have been received to continue them.



Students participating in experiments

Kao Corporation Shanghai plans to further deepen its roots in the local community through activities such as these, and continue undertaking activities that allow it to cooperate in the development of the local community.



## Corporate Citizenship Activities in FY 2006 (Domestic Kao Group)

Area	Program	Activities
Environmental Conservation	Kao Creating Forests for Everyone Campaign	<ul style="list-style-type: none"> <li>January 25, 2007: Seventh session of the Creating Forests for Everyone selection committee held. Total grants of 23 million yen to 40 organizations. Project grants: 135 organizations applied; 27 organizations selected. Start-up grants: 38 organizations applied; 13 organizations selected.</li> </ul>
	KIDS ISO Program	<ul style="list-style-type: none"> <li>Environmental education program for children. Donated 500 copies of a textbook to be used in school classes, and 6 Kao staff cooperated as instructors.</li> </ul>
Education	Kao Teacher Fellowship (Overseas Field Research Program)	<ul style="list-style-type: none"> <li>47 teachers applied; 11 teachers participated (during summer vacation in July and August 2006)</li> <li>Project participation: India (health of mothers and children), Australia (echidna, goanna), Iceland (glaciers), North America (island ecosystems), North America (orca), Kenya (mangrove)</li> </ul>
	Co-sponsoring the Japan Science & Engineering Challenge (JSEC2006) hosted by Asahi Shimbun	<ul style="list-style-type: none"> <li>A worldwide competition for high school students to encourage independent research in science and technology. The Kao Award was given for research on "The impact of eutrophication on the interspecies relationship between <i>Oryzias latipes</i> and <i>Gambusia affinis</i>" performed by Asa High School in Yamaguchi Prefecture.</li> </ul>
	Science Experiment Classes	<ul style="list-style-type: none"> <li>June 15, 2006: Toin High School, Wakayama Prefecture</li> <li>August 2, 2006: Hiroshima Prefectural Fukuyama High School</li> <li>December 21, 2006: Soma High School, Fukushima Prefecture</li> <li>January 26, 2007: Omiya Musashino High School, Saitama Prefecture (Science Partnership Program)</li> <li>March 30, 2007: Saitama Prefecture Association of Physics and Chemistry Education in High School, Chemistry Sub Committee</li> <li>Other, July 28, 2006: Kashima Plant tour; February 4, 2007: Gunma Children's Museum</li> <li>Provision of content to the Saturday Experiment Class of the Science Museum</li> </ul>
Community	Kao Family Concerts	<ul style="list-style-type: none"> <li>October 26, 2006: Kao Family Concert in Sakata held, featuring cellist Yoko Hasegawa and pianist Yuko Nakamichi. Attendees numbered 950.</li> <li>March 11, 2007: Kao Family Concert in Tochigi held, featuring violinist Narimichi Kawabata. Attendees numbered 850.</li> </ul>
	Donation of Kao products to welfare facilities	<ul style="list-style-type: none"> <li>Donations made: Consumer products to 444 welfare facilities; Econa Cooking Oil to 82 NPOs providing meals services.</li> </ul>
Promotion of a Barrier-Free Society	Donation of barrier-free video	<ul style="list-style-type: none"> <li>Donated educational video produced together with The Accessible Design Foundation of Japan to 62 schools. Lent the same video to 52 organizations.</li> </ul>
	Braille seals	<ul style="list-style-type: none"> <li>Distributed Braille seals to help the visually disabled distinguish household products and cosmetics products that have similar shapes but must be used in different ways. (986 seals for household, 1179 for cosmetics)</li> </ul>
	Audio information for visually disabled people	<ul style="list-style-type: none"> <li>Distributed 1,129 "Kao Voice Guide of Everyday life" DAISY CDs, 250 "Science in Everyday Life, Laundry" CDs and others</li> </ul>
	Support for art appreciation programs for the visually disabled	<ul style="list-style-type: none"> <li>Education program research and promotion activities undertaken together with Gallery TOM. Guest speakers discuss education programs for the visually impaired in various countries. In fiscal year 2006, Ms. Hoelle Corvest of the Cite des Science et de l'Industrie spoke.</li> </ul>
	Co-sponsorship of workshop for hearing-disabled children	<ul style="list-style-type: none"> <li>Held 17 workshops in 10 Tokyo schools for the deaf-mute, schools for handicapped children, and nursery facilities to help hearing-disabled children discover the joy of sound.</li> </ul>
Fine Art	Sponsored the 4th Tokyo Music Competition	<ul style="list-style-type: none"> <li>In 2006, the competition was held in two categories, piano and strings. Entrants numbered 95. Five people were presented with awards after first and second round selections and final judging, which was open to the public.</li> </ul>
	Support for the Japan Association of Art Museums	<ul style="list-style-type: none"> <li>30 art exhibitions toured a total of 59 museums. Two curators were dispatched overseas. A research grant was awarded to one curator. Five local museum activity grants were awarded. Six exhibition catalogue awards were presented.</li> </ul>
Employee Participation Activities	Heart Pocket Club	<ul style="list-style-type: none"> <li>Members numbering 1,593 donated to 25 NPO/NGOs and 2 disasters.</li> </ul>
	World Culture Festival	<ul style="list-style-type: none"> <li>Co-sponsored a food-based international cooperation program together with Kikkoman Corporation and Asahi Breweries, Ltd. 33 employees participated.</li> </ul>

## Corporate Citizenship Activities in FY 2006 (Overseas Kao Group)

Kao Group companies outside Japan	Activities	Kao Group companies outside Japan	Activities
Kao (China) Holding Co., Ltd.	<ul style="list-style-type: none"> <li>Donation of products to charitable organizations</li> </ul>	Kao Indonesia Chemicals	<ul style="list-style-type: none"> <li>Donations to the victims of the Mid Java Earthquake</li> <li>Donations to local orphans and elderly people</li> </ul>
Kao (Taiwan) Corporation	<ul style="list-style-type: none"> <li>Donation of products to orphanages</li> <li>Donation of safety vests for use by "Guard Mothers" at local primary schools</li> </ul>	Kao Specialties Americas LLC.	<ul style="list-style-type: none"> <li>Participated in creating flowerbeds at local primary schools</li> </ul>
Kao Industrial (Thailand) Co., Ltd. Kao Commercial (Thailand) Co., Ltd.	<ul style="list-style-type: none"> <li>Donation to primary school children in poor areas</li> <li>Donation to flood victims</li> </ul>	Kao Chemicals GmbH	<ul style="list-style-type: none"> <li>Purchases of products created by students of a school for the blind</li> </ul>
P.T. Kao Indonesia	<ul style="list-style-type: none"> <li>Donations to the victims of the Mid Java Earthquake</li> </ul>	Kao Corporation S.A. (Spain)	<ul style="list-style-type: none"> <li>Support for the issuance of a community magazine</li> <li>Support for a local children's soccer team</li> </ul>
Molton Brown Ltd.	<ul style="list-style-type: none"> <li>Donations to charities for children</li> <li>Donations for cancer research</li> </ul>	Fatty Chemical (Malaysia) Sdn. Bhd.	<ul style="list-style-type: none"> <li>Donation of soap to schools, hospitals, public institutions, and other organizations</li> </ul>
Kao Brands Co.	<ul style="list-style-type: none"> <li>Participation as volunteers in local primary school literacy program (See page 47)</li> <li>Donation of products to an international anti-poverty program</li> </ul>	Pilipinas Kao, Incorporated	<ul style="list-style-type: none"> <li>Repair activities for local primary schools</li> <li>Assistance for health check-ups for local residents</li> </ul>

# Environmental Activities

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From the product planning and development stage through use/consumption and disposal, Kao endeavors to conserve the global environment in all aspects of its business activities.

### Kao's products and their impacts on the environment

Kao's products are made mainly from vegetable oil and fat, and fossil resources. Most of our products are used by consumers on a daily basis, so we work to use resources as efficiently as possible when we design, develop, and manufacture products, and pursue technologies that will reduce our use of resources and energy.

As a company that handles chemical substances, we are very concerned with the impacts they have in product lifecycles, but we must also be conscious of the ways in which chemicals affect human health and the ecosystem in all of our business activities, and act accordingly. Kao has created a strict chemical substances management system, is working to reduce the environmental burden of its product development and production activities, and strives to strike a good balance between business development and the reduction of its environmental burden.

### Environmental burden — our primary concerns

#### 1 Greenhouse gas emissions

Production and distribution activities produce greenhouse gases such as CO<sub>2</sub>. Kao is working to reduce greenhouse gas emissions in all phases of its business activities — from research and development to sales.

#### 2 Chemical substances management

Using its own comprehensive management system for chemical substances (See page 27), Kao is reducing its use and emissions of both chemical substances subject to the PRTR Law and volatile organic compounds (VOC).

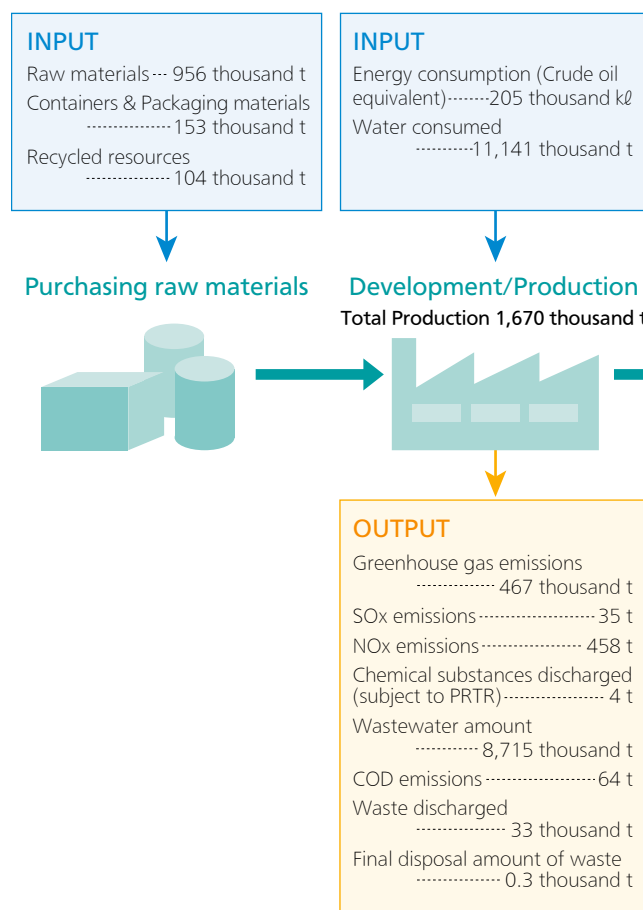
#### 3 Industrial waste

Kao is reducing final disposal amounts by effectively using by-products and waste from products to the extent possible. We define zero emissions as final disposal amounts that are 0.5% or less of generated waste. One of our goals was to achieve zero emissions at all of its domestic factories by fiscal year 2006.

#### 4 Containers and packaging materials

Kao continues to promote the 3Rs (Reduce, Reuse, and Recycle) for containers and packaging.

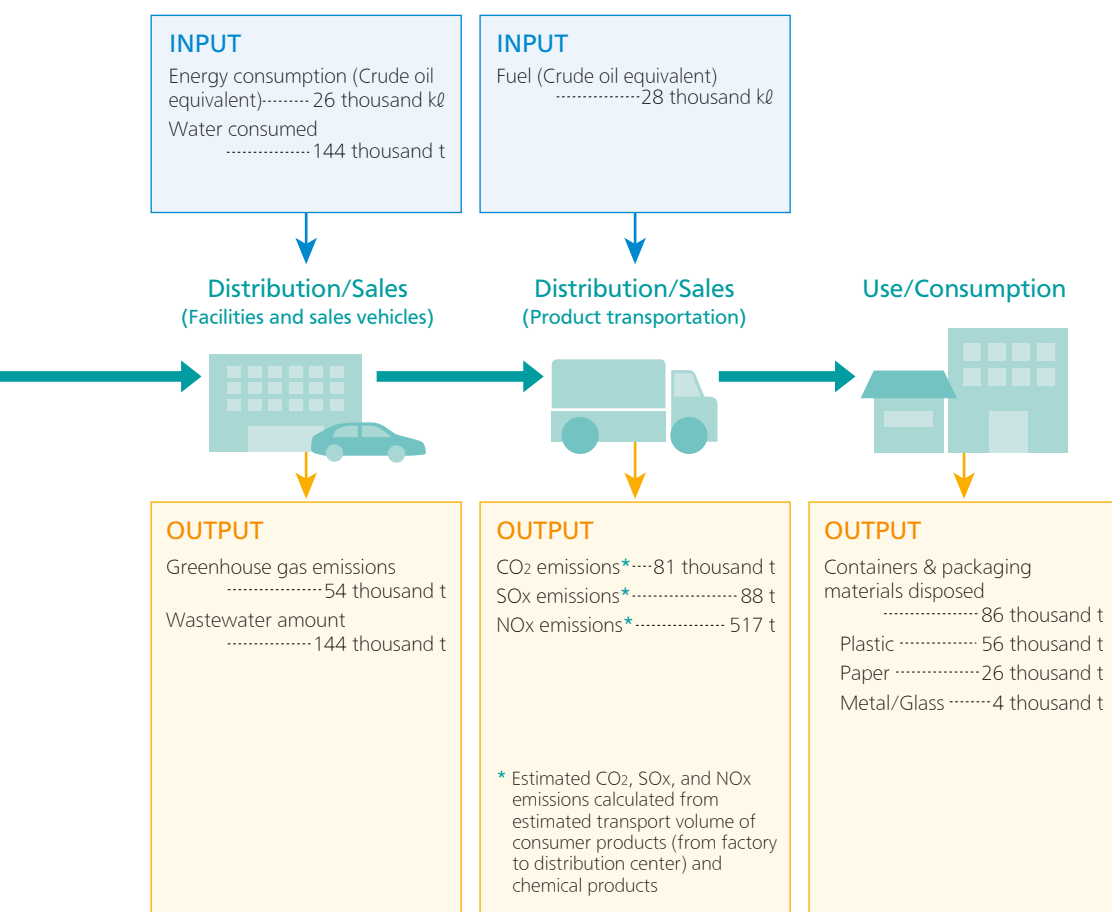
### FY 2006 Business Operations and Environmental Burden



### Definitions of Business Operations and Environmental Burden Indicators

#### INPUT

- Raw materials: The amount of raw materials directly used to manufacture products (excluding packaging materials and fuel)
- Containers and packaging materials: Total amount of containers, packaging materials, and cardboard used for products that have been sold
- Recycled resources: Of the waste generated from production and research activities, the amount that is recycled within Kao
- Energy input (Development, production): Amount of energy consumed in production activities (excluding energy that is used in non-production activities such as administrative and research activities)



- Water consumed: Total amount of water consumed
- Energy consumption (Distribution, sales): Amount of energy consumed by distribution and sales offices, and other facilities, and by vehicles (used for sales) (Actual energy consumed in sales activities cannot be determined in the case of some leased buildings. For these cases, estimates have been made based on per person consumption calculated based on collected data. The data collection rate is 64%.)
- Fuel: Crude oil consumption based on estimates of shipped volumes of consumer (from factory to distribution facility) and chemical products

#### OUTPUT

- Greenhouse gas emissions: Amount (CO<sub>2</sub> equivalent) of greenhouse gas (the six gases specified in the Kyoto Protocol) generated from business activities
- SO<sub>x</sub> emissions: Total amount of SO<sub>x</sub> emissions from smoke and soot emitting facilities
- NO<sub>x</sub> emissions: Total amount of NO<sub>x</sub> emissions from smoke and soot emitting facilities
- Chemical substances emissions: Amount of substances subject to the PRTR Law discharged into the air and water
- Wastewater amount: Total quantity of wastewater discharged from production plants, distribution and sales offices, and other facilities
- COD emissions: Figure calculated by multiplying the amount of wastewater by COD concentrations in the wastewater
- Waste discharged and final disposal amount of waste: The amount of production waste that is sold or entrusted as waste or recyclable material to waste treatment companies, and the final amount of waste disposed of
- Containers and packaging materials disposed of: The total amount of containers and packaging materials (excluding cardboard) used for products that have been sold

## To lower its environmental burden, Kao has established its 6 priority items and FY 2010 Targets and is continuously and effectively moving forward with environmental conservation activities.

### Fiscal year 2006 results and directions for the future

Kao has established six areas — energy-saving, global warming prevention, waste reduction, chemical substance emission reduction, green purchasing, and CSR procurement — as priorities and set numerical targets to be achieved by fiscal year 2010.

In fiscal year 2006, Kao reviewed the methods it used to calculate greenhouse gas emissions recalculated retroactively to 1990, in the light of the revision of the Law Concerning the Promotion of the Measures to Cope with Global Warming. As a result, we determined that, although we had achieved all other numerical targets, we had not met targets for

greenhouse gas emissions.

Kao will establish new targets based on what it has achieved and will put together new measures for those items where its efforts have been inadequate. Regarding global warming in particular, Kao is aiming to achieve targets by moving forward with integrated energy-saving activities and fuel conversion measures, based on the national government's plan for achieving Kyoto Protocol targets.

As for waste reduction targets, Kao will work toward zero emissions by setting new numerical targets as it achieves those already established and consider targets for reducing its use of containers and packaging materials.

**HP** Environmental burden data for domestic and overseas (Asia, Europe, U.S.) production plants  
<http://www.kao.co.jp/en/csr/report/>

### Environmental Targets and Results

Priority item	FY 2006 target	FY 2006 result	FY 2007 policy and target	FY 2010 target
Energy conservation	Reduce energy consumption during production activities to 76 in basic unit index*1 as compared to 1990 level	<ul style="list-style-type: none"> <li>Reduced to 75 in basic unit index compared to 1990 level</li> <li>Target achieved because of improvements in operating method, facility and equipment efficiency, and other factors (130 improvements in all)</li> </ul>	<ul style="list-style-type: none"> <li>Steadily implement energy conservation activities</li> <li>Maintain 75 in basic unit index compared to 1990 level</li> </ul>	Reduce to 72 in basic unit index compared to 1990 level
Global warming prevention	Reduce greenhouse gases emissions*2 to 69 in basic unit index as compared to 1990 level	<ul style="list-style-type: none"> <li>Reduced to 71 in basic unit index as compared to 1990 level</li> <li>Calculation method was revised*3 back to 1990, so target was not achieved despite promotion of fuel conversion, and switching from private power generation to electricity purchasing, etc.</li> </ul>	<ul style="list-style-type: none"> <li>Promote further energy conservation and fuel conversion</li> <li>Reduce to 68 in basic unit index as compared to 1990 level</li> </ul>	Reduce to 65 in basic unit index compared to 1990 level
Waste material reduction	All plants in Japan achieve zero emissions*4	Achieved at all plants	<ul style="list-style-type: none"> <li>Maintain zero emissions at all plants</li> <li>Reduce waste generation 0.5% per unit production compared to prior year level</li> </ul>	<ul style="list-style-type: none"> <li>Reduce total final disposal amount for all plants to 150 tons or less and achieve zero emissions*5 under the new definition</li> <li>Reduce waste generation 0.5% per unit production compared to prior year level</li> </ul>
Reduction of chemical substance emissions	Chemical substances subject to the PRTR Law	Achieved	<ul style="list-style-type: none"> <li>Maintain emissions at 1 ton or less for each chemical at respective plants</li> </ul>	<ul style="list-style-type: none"> <li>Maintain emissions at 1 ton or less for each chemical at respective plants</li> </ul>
VOC*6 chemicals	Emission of each chemical from respective plants to be maintained at 5 tons or less	Achieved	<ul style="list-style-type: none"> <li>Maintain emissions at 5 tons or less for each chemical at respective plants</li> </ul>	<ul style="list-style-type: none"> <li>Maintain emissions at 1 ton or less for each chemical at respective plants</li> </ul>
Green purchasing*7	Green Purchasing Ratio for copy paper and other stationery to be 90% or higher	Achieved (Green Purchasing Ratio: 94%)	Maintain at 90% or higher	100%
CSR procurement*8	Green Procurement Ratio*8 to be 90% or higher	Achieved (Green Procurement Ratio: 99.6%)	Maintain at 90% or higher	100%

\*1 Basic unit index: Amount of per unit value-added production output. Index represented with the 1990 value defined as 100. Value added production output is the amount that can be obtained by excluding the variable manufacturing cost from the production output on the basis of selling price.

\*2 Greenhouse gas emissions: CO<sub>2</sub> equivalent emissions of six greenhouse gases specified in the Kyoto Protocol.

\*3 Calculation method revision: To achieve consistency with the Ministerial Ordinance Concerning the Estimations of Greenhouse Gas Emissions Associated with the Business Activities of Specific Waste Generators and the Calculation and Reporting Manual for Greenhouse Gas Emissions Ver. 1.2 when calculating energy consumption, the calculation approach given in that manual and the same heat quantities were adopted. For city gas, volume calculations were previously based on ambient temperature and 1 atmosphere, but were changed to include conversion to standard conditions of the 0°C and 1 atmosphere. These revised formulas were used to recalculate consumption since 1990.

\*4 Zero emissions: Reduction of the annual final disposal amount to 0.5% or less of generated waste by weight.

\*5 Zero emissions under the new definition: Reduction of the annual final disposal amount to 0.1% or less of generated waste by weight.

\*6 VOC: Abbreviation for Volatile Organic Compounds. Specifically, Kao defines the 100 substances listed in the Notice of Director-General, Environmental Management Bureau, Ministry of the Environment (June 17, 2005) as VOC.

\*7 Green purchasing: The purchase of products that have less impact on the environment (green products) preferentially at the time of purchasing office supplies and machinery, taking the entire lifecycle of the item to be purchased into account. The ratio of the amount of green purchasing to the total amount of purchasing is referred to as the Green Purchasing Ratio.

\*8 CSR procurement/Green Procurement Ratio: Giving preference to suppliers that consider their responsibilities to the environment and society, and preferentially selecting products (green products) with lower environmental burdens, when purchasing goods necessary for production activities. For CSR procurement, suppliers are assigned the following ranks in environmental protection assessments: A (Outstanding use of an Environmental Management System (EMS)), A1 (Planning to obtain ISO14001 or some other standard certification), B (Uses an EMS), and C (Needs to build an EMS). The Green Procurement Ratio is the ratio of supplier factories that have attained a ranking of B or better in an environmental protection assessment. Environmental protection assessment methods are separately specified in the CSR Procurement Guidelines.



Kao is addressing the problem of global warming through proactive technology development, production process improvements, and other creative measures.

## Efforts in research and development

Kao's Research & Development division has positioned the reduction of environmental burden as a key theme for basic technology research. Meanwhile, at the product development stage, environmental consideration, such as resource and energy savings, and safety are evaluated as key factors in product Life-Cycle Assessments and chemical substance risk assessments.

In addition, Kao is pouring resources into research not only for reducing direct CO<sub>2</sub> emissions from its production plants but also for the use of biomass, which can lead to lower CO<sub>2</sub> emissions from society as a whole.

### Development of technology to reduce CO<sub>2</sub> emissions

To reduce CO<sub>2</sub> emissions, Kao is pushing forward with the development of processes that are highly energy efficient and of industrial products like biodegradable plastics that use materials from carbon-neutral\* biomass. The results of this research are applied in the development of individual products and new chemical substances that excel in terms of environmental consideration and safety. To date, they have contributed to the development of a manufacturing process of functional composite powder using supercritical carbon dioxide, environmentally conscious modified resin/film, and pulp molding technology to produce hollow moldings.

#### \* Carbon neutral

A concept explaining part of the carbon cycle. As with fossil fuels, plants generate CO<sub>2</sub> when they are burned. However, they absorb CO<sub>2</sub> in the air through photosynthesis in the process of growth. Therefore the balance is zero.

### Environmentally conscious products that contribute widely to industry

Kao is promoting the development of industrial products that lower the environmental burden of industry.

One of these products is the *EG Runner*, a casting runner that can be used with molten iron at temperatures of 1,500°C and higher. *EG Runner* is made of recycled paper, turn to ash once they are used, and make possible both the use of recycled resources and a significant reduction in waste material. (See page 13)

## Efforts in production processes

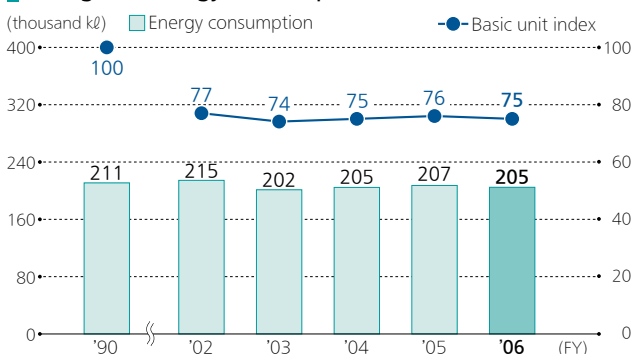
Kao is introducing energy-saving equipment, streamlining production processes, and engaged in a variety of other activities aimed at making its production processes more energy efficient. For fiscal year 2006, these efforts resulted in an overall energy use reduction equal to 2,300 kl of crude oil, compared to fiscal year 2005. They also improved our energy basic unit index by 0.9 points on an annual basis. Kao aims to continue its energy-saving activities and achieve its numerical targets.

### Reduction in greenhouse gas emissions through fuel conversion

To reduce greenhouse gas emissions, Kao holds down its use of power generated internally with heavy fuel oil and instead uses purchased power with low CO<sub>2</sub> emissions. This reduced our CO<sub>2</sub> emissions by 7,500 tons compared to fiscal year 2005 and cut our fiscal year 2006 greenhouse gas emissions by 9,100 tons totally. Furthermore, it improved our basic unit index, by 1.4 points compared to fiscal year 2005.

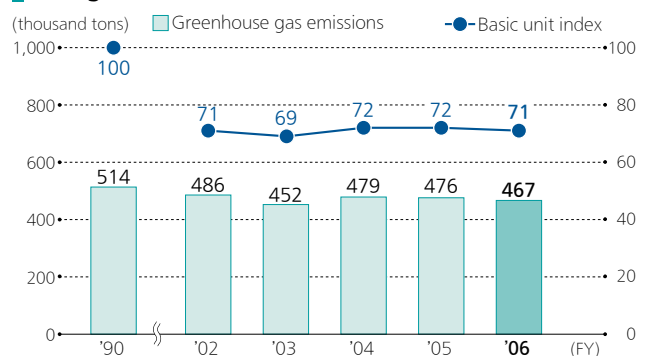
In fiscal year 2007, we are promoting further conversions to natural gas in preparation for the Kyoto Protocol's first commitment period, which runs from fiscal year 2008 through fiscal year 2012. We are also keeping alive the option of acquiring greenhouse gas emission credit.

### Changes in Energy Consumption of Production Activities



\*To bring energy consumption into line with the Ministerial Ordinance Concerning the Estimations of Greenhouse Gas Emissions Associated with the Business Activities of Specific Waste Generators and the Calculation and Reporting Manual for Greenhouse Gas Emissions Ver. 1.2, heat quantities specified in the manual were used. For city gas, calculations were previously based on conditions of ambient temperature and 1 atmosphere, but were changed to include conversion to standard conditions of 0°C and 1 atmosphere. These revised formulas were used to recalculate consumption since 1990.

### Changes in Greenhouse Gas Emissions



\*Greenhouse gas emissions (CO<sub>2</sub> equivalent) were recalculated based on the Ministerial Ordinance Concerning the Estimations of Greenhouse Gas Emissions Associated with the Business Activities of Specific Waste Generators and the Calculation and Reporting Manual for Greenhouse Gas Emissions Ver. 1.2. Regarding electricity and city gas in particular, the emissions coefficients of individual suppliers were used.

## Efforts in offices, distribution, and sales

Kao is actively working to prevent global warming not only in its product development and production facilities but also in its offices. In distribution and sales, activities are being pursued in cooperation with retailers and business partners.

### Efforts in distribution

To reduce environmental burden at the distribution stage, Kao is building and operating efficient distribution systems, instituting modal shifts from truck transportation to low-environmental-burden rail and ship transportation, and working with other companies on initiatives like cooperative transport.

In fiscal year 2006, we reduced our energy consumption and CO<sub>2</sub> emissions by improving transportation efficiency for some feminine and baby products through the implementation of a new pallet-less truck transportation system. Additionally, with the April 2007 implementation of the revised Energy-Saving Law, we introduced a system for calculating fuel consumed for transportation. Moving ahead, we plan to pursue further energy-saving measures.

### Participation in the “Team Minus 6%” campaign

Since 2005, Kao has been participating in the “Team Minus 6%” national project to prevent global warming. Through this project, fiscal year 2006 electricity consumption in offices was reduced by 628,000kWh (approx. 4%) compared to fiscal year 2004, which predated the beginning of the project. This amount of energy savings is equivalent to 178kl of crude oil and 264 tons of CO<sub>2</sub>.

Kao is also encouraging consumers by creating POP signs explaining methods for cleaning “Cool Biz” clothing items. This gives consumers better understanding of “Cool Biz”.



POP sign informs consumers that they can keep Cool Biz clothing items looking freshly ironed by using *Keeping Style Care*

## TOPICS

### Wakayama Plant recognized in the 4th Japan Cogeneration Center Awards

In May 2006, the Wakayama Plant received the Japan Cogeneration Center's President's Award in the industrial division of the 4th Japan Cogeneration Center Awards. The Wakayama Plant reuses high temperature air from its gas turbine generator as combustion air for its boilers, to produce high and low pressure steam, and in other ways, promotes the use of waste heat. The awards committee praised the Wakayama Plant for its wide-ranging environmental protection activities, which go beyond saving energy. Examples include the use of city gas, which has a low CO<sub>2</sub> emission coefficient; the development of technology that allows the plant to continue operating



Japan Cogeneration Center representatives and Kao employees at the award ceremony

even if turbines and boilers stop operating; and a method for eliminating foul odors from gases emitted from the plant's chemical facilities.

### Transportation Modes and Exhaust Gas Emissions (FY 2006)

Transportation mode	Transportation Quantity Ratio by Mode (%)	CO <sub>2</sub> (t)	SOx (t)	NOx (t)
Consumer products				
Truck	62	58,535	9	409
Rail	14	2,026	1	1
Ship	24	6,230	70	9
Total	100	66,791	80	419
Chemical products				
Truck	79	13,951	2	97
Rail	10	123	0	0
Ship	11	260	6	1
Total	100	14,334	8	98

- Transportation quantity=Weight of transported goods multiplied by distance
- CO<sub>2</sub> emissions were calculated using the emission coefficients required by the Ministerial Ordinance Concerning the Estimations of Greenhouse Gas Emissions Associated with the Business Activities of Specific Waste Generators and emission coefficients contained in the Calculation and Reporting Manual for Greenhouse Gas Emissions (Ministry of the Environment, Ministry of Economy, Trade and Industry).
- SOx emissions were calculated using emission coefficients based on regulatory values and standards for individual types of fuels, and LCI data for electricity.
- NOx emissions were calculated using Eco Program coefficients and LCI\* data for electricity.

#### \*LCI

Life Cycle Inventory. Information on resources necessary for manufacturing products and on atmospheric emissions and other environmental burdens on a product unit basis.

## Kao ensures safety and security from all perspectives by using its own Comprehensive Management System for Chemicals, which integrates regulatory, and management systems, etc.

### Reduction of chemical substance emissions

Kao's Comprehensive Management System for Chemicals combines a System for Supporting New Product Development, Chemical Regulatory Compliance Information, an MSDS Management System, and an Export Support Tool. We use our Comprehensive Management System for Chemicals to pursue integrated chemical management and reduce chemical substance emissions. Kao divides chemical substances into the following four ranks.

- **Prohibited chemical substances:** substances that Kao prohibits usage (PCB, asbestos, etc.)
- **Limited use chemical substances:** substances that are being phased out in the near future (Substances that deplete the ozone layer, specified heavy metals, etc.)
- **Chemical substances requiring careful handling:** substances that must be carefully handled based on the risks they pose (Chemicals specified in the PRTR Law, poisonous and deleterious substances, etc.)
- **Other substances:** substances other than the above

### Promoting low-environmental-burden procurement

Kao conducts Environmental Management System (EMS) evaluations of the factories of key suppliers based on the Green Procurement Guidelines established in April 2004.

In fiscal year 2006, we increased by 108 the number of domestic factories we evaluate, raising the total to 540. The results indicated that 99.6% of them met standards. Kao will continue to encourage those factories not meeting standards to establish EMSs and improve their operations.

\* In January 2007, Kao prepared standards to promote CSR procurement, which promotes CSR throughout the supply chain. Kao is evaluating domestic and overseas suppliers on not only compliance with green procurement standards but also social responsibility standards such as regulatory compliance, corporate ethics, efforts to eliminate discrimination and illegal labor practices.

### Reducing emissions of chemical substances subject to the PRTR\* Law

Kao achieved its fiscal year 2006 target of maintaining emissions of each chemical from respective factories at one ton or less, holding total discharges into the atmosphere and the water to four tons.

We plan to keep meeting our objectives by continuing our activities in this regard.

#### \* PRTR

Pollutant Release and Transfer Register. The PRTR Law is intended to encourage companies to voluntarily improve their management of chemicals and, thereby, prevent obstacles to protecting the environment.



Lists of the emissions of chemical substances subject to the PRTR Law

<http://www.kao.co.jp/en/csr/report/>

### Reducing VOC emissions

Kao has no facilities subject to VOC\* regulatory control, but voluntarily checked its VOC emissions for 100 substances. Fiscal year 2006 results indicated that we discharged a total of 11 tons of these substances into the air, and met our target of maintaining emissions of each chemical from respective factories at five tons or less.

In fiscal year 2007, we will examine measures for holding down our use of substances that produce VOC emissions and for eliminating emissions, so that we can continue to maintain emissions of each chemical from respective factories at five tons or less and eventually cut them to one ton or less in fiscal year 2010.

\* VOC Volatile Organic Compounds

### MSDS preparation and carrying of Yellow Cards

Kao provides customers with a Material Safety Data Sheet\*<sup>1</sup> (MSDS) for each industrial product it sells to them. Our MSDS Management System provides MSDSs in multiple languages and allows MSDSs to be viewed and printed via the Internet at distribution centers.

When chemicals are transported by tank truck, we provide the transportation company with documentation containing information on how to respond in an emergency and require drivers to carry Yellow Cards\*<sup>2</sup>. For chemical substances that are transported in drums, 18ℓ cans in small, mixed volumes, we affix to each container a Container Yellow Card bearing emergency response information.

#### \*<sup>1</sup> MSDS

A Material Safety Data Sheet provides the names of substances included in the subject product, toxicity information, handling precautions, and other information necessary for safely and appropriately handling the subject chemical product.

#### \*<sup>2</sup> Yellow Card

A Yellow Card provides toxicity information, emergency measures, parties to contact in case of an accident, and other information on the subject chemical substance. It must be carried by transportation personnel during transportation and is intended to facilitate the rapid provision of information on environmental, safety, health, and handling precautions to third parties and, thereby, prevent secondary accidents during transportation.

Kao has achieved zero emissions at all of its domestic production plants. Going forward, we will improve our activities through the implementation of our Waste and Recycling Governance System and other measures.

### Achievement of zero emissions at all domestic production plants

Kao is working to reduce the generation of waste in its production activities by decreasing the amount of water consumed to wash tanks, optimizing the size of mixing tanks to cut waste fluids and reduce the amount of cleaning water necessary, and creating more refined production plans. As for waste material generated despite these efforts, we are working to put as much of this material as possible to effective use either within our plants or by enlisting the services of outside companies.

We established zero emissions\* as a goal in fiscal year 2004 and achieved it for all domestic plants in fiscal year 2006, when we cut the final disposal amount for all of our plants to 280 tons, a reduction of 57% compared to the prior year. Now, the final disposal ratio for all domestic plants is only 0.20%.

Moving ahead, we will continue to cut the final disposal amount for domestic plants, with the goal of reducing the absolute final disposal amount to 150 tons or less by 2010.

#### \* Zero emissions

Kao defines "zero emissions" as final disposal amounts that are 0.5% or less of the total annual waste generated by weight.

### Recycling activities at offices not involved in production

Kao's Kayabacho and Osaka Offices are pursuing 3R activities in regard to general waste materials, promoting the separation and recycling of paper, plastic, and cardboard.

Distribution affiliates are actively implementing the recycling of plastic and cardboard waste materials left after products are transported and delivered. Regarding plastic materials in particular, all facilities are collecting and sorting out-dated collapsible plastic containers, consigning waste plastic to recyclers, and pursuing other recycling activities.

### Introduction of the Waste and Recycling Governance System

With waste processing and recycling governance taking on increased importance, Kao has developed its Waste and Recycling Governance System for the integrated management of agreements with outside service providers, industrial waste management manifests, and data on waste volume. Implementation of this system got underway at factories operated by nine factories of both Kao and its affiliates in October 2006 and in some nonproduction offices and other affiliates in April 2007.

This system, by permitting relevant parties to share information on waste processors and processing agreements, will boost transparency and reduce the risks of illegal dumping and inappropriate processing by waste processors. Additionally, centralized management of manifest processing will enhance traceability and promote appropriate processing.

#### Voice

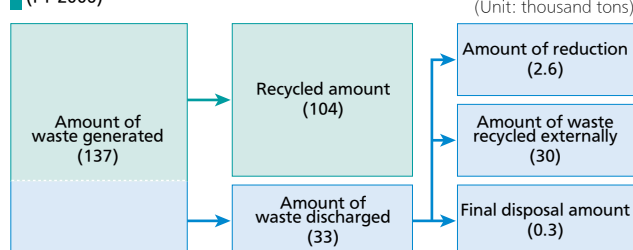
#### Introduction of electronic manifests at the Sakata Plant

Hitomi Chubachi  
(Production Department, Sakata Plant)



At the Sakata Plant, electronic manifests were partially introduced in July 2006. Shifting to electronic manifests has not only eliminated the need for a large volume of documents but also enhanced traceability. Employees have commented that the ability to process manifests at any time on a computer has made timely confirmation of manifest status possible, and outsourcing suppliers have praised the electronic manifests for the greater convenience they offer.

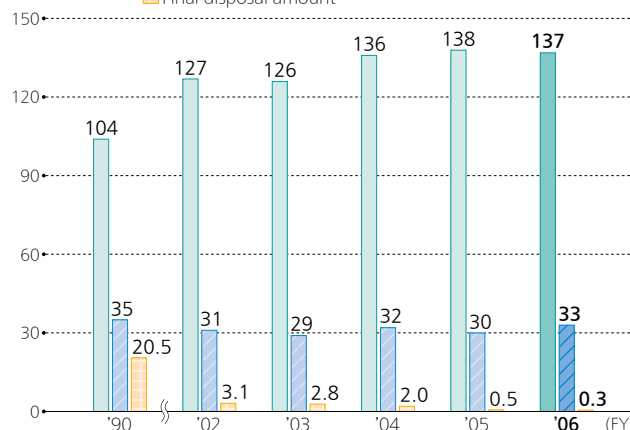
### Amount of Waste Generated and Treatment Flow (FY 2006)



- Amount of waste generated: Undesirable substances and defective products generated from the production stage (including valuable resources such as used paper and metals, and items that can be used at other plants.)
- Recycled amount: Waste that are reused or recycled as resources at plants (including thermal recycling).
- Amount of waste discharged: Undesirable substances and defective products, incinerated ash, used paper, and metals that are removed from plants.
- Amount of waste recycled externally: Waste that is recyclable or reused as resources after treatment (including thermal recycling).
- Final disposal amount: Waste that cannot be used in any way and is safely buried in landfill sites.

### Changes in Waste Amounts

(thousand tons) Generated amount Discharged amount Final disposal amount



While Kao strives to enhance product value through containers and packaging materials, it is also working to apply the 3Rs to these items considering their recycling and reusing.

## Effective Utilization of Resources and the 3Rs

Until contents are used up, containers and packaging materials, as parts of products, protect contents and preserve quality during transportation, provide product usage information, and perform other important roles and functions. Kao performs research and development to create containers and packaging materials that fulfill these roles and functions, and is actively pursuing 3R activities aimed at recycling and reusing containers and packaging materials.

### 1. Reduce:

concentrate product contents and create compact containers and packaging materials

### 2. Reuse:

promote the reuse of containers and packaging materials by offering refill and replacement products

### 3. Recycle:

recycle used containers

## Efforts to reduce and reuse

Kao is working to reduce its use of containers and packaging materials by actively developing products that are compact and product refills and replacements. In fiscal year 2006, we introduced *Bioré u Bath Milk*, simultaneously began selling refills for this product, and introduced product refills for *Success Shampoo*.

Kao uses advanced container design technology to create tough containers that protect contents from impacts and preserve quality, while also reducing our plastic usage. We are also continuing to reduce the amount of resin we use for



### Reduce

By increasing the performance of products and making them more compact, Kao is decreasing the amount of product needed for each use and reducing material and energy usage, and waste.



### Reuse

Product refills make it possible to use shampoo and liquid body cleanser containers over and over and, thereby, help to conserve resources and reduce waste.

containers. In fiscal year 2006, we cut the amount of plastic we use in bottles for our *Haiter*, *Kitchen Haiter*, and *Healthya* products and reduced the thickness of *Healthya* labels, decreasing our use of plastic for these products by 190 tons. That figure equates to 371kl of crude oil.

Regarding the cardboard we use for transporting our products, we have cut weight per unit area without sacrificing functionality, such as strength. This new cardboard allowed us to reduce our cardboard usage by 80 tons annually.

Kao is reducing its use of containers and packaging materials through these 3R activities, but introductions of new products and higher sales of existing products in fiscal year 2006 increased our container and packaging material usage by 7,900 tons compared to fiscal 2005. Kao, however, will remain steadfast in its efforts to reduce its use of containers and packaging materials.



Compact-type products, refill and replacement products and their conversion rates

<http://www.kao.co.jp/en/csr/report>

## TOPICS

### Formulating an industry-wide voluntary action plan

To promote effective resource usage, the Japan Soap and Detergent Association, of which Kao is a member, has created an industry-wide voluntary action plan with the goal of reducing the amount of plastic (basic unit index) used in containers and packaging materials 30% (compared to the figure for fiscal year 1995) by fiscal year 2010. In implementing this plan, actions such as promoting greater use of refill and replacement products; designing containers that have thinner walls and weigh less; offering contents in concentrated, compact versions; and other activities are being pursued in eight product categories, which include body washes, hand cleaning agents, shampoos/conditioners, liquid laundry detergents, fabric softeners, dishwashing detergent, household cleansers, and bleaches/mildew removers. Kao, which offers these products, is taking part in this plan and working to achieve targets.

## Changes in Container and Packaging Materials used

(Unit: tons)

	FY2002	FY2003	FY2004	FY2005	FY2006
Plastic	42,800	46,800	49,000	49,200	55,700
Paper	21,000	26,000	25,800	26,100	25,600
Cardboard	56,400	60,300	64,300	65,600	67,700
Others	3,100	3,300	3,600	3,800	3,600
Total	123,300	136,400	142,700	144,700	152,600



Kao is promoting effective water resource usage and the preservation of biodiversity, and pursuing a variety of other environmental protection activities that are closely tied to its business activities.

### Circulatory usage of water resources

Each of Kao's factories uses water as a product component, to clean and cool equipment, and for human needs. To use water efficiently, water that has been used for cleaning or other purposes is purified and reused.

In fiscal year 2006, production rose on an annual basis, but we still succeeded in reducing our water consumption by 496 thousand tons and our wastewater output by 766 thousand tons. These reductions were primarily the result of an improved wastewater treatment method that was implemented in fiscal year 2006 and held down our well water usage, and the Wakayama Plant's installation of improved soot and dust control equipment, which reduced water usage.

### PCB disposal

Polychlorinated biphenyls (PCBs) are stored under strict supervision at the Wakayama Plant and the Tokyo Plant. In 2005, we requested the Japan Environmental Safety Corporation to properly treat this material and are currently waiting for this to happen.

### Compliance with laws and response to regulations

In April 2005, there were exhaust gas emissions that temporarily and slightly exceeded the standard level for soot and dust at the Wakayama Plant. To resolve this problem, we installed a continuous monitoring system and undertook fundamental improvements to plant facilities. Meanwhile, the

BOD level at the Tokyo Plant had temporarily exceeded sewage standards in two consecutive years, and we took measures, including monitoring and management system enhancements and facility improvements, to prevent a recurrence.

As a result of these measures, SOx, NOx, and soot and dust emissions; and BOD, COD, phosphorus, and nitrogen levels in wastewater were all within legal limits at all domestic Kao plants in fiscal year 2006.

### Measures to deal with soil contamination

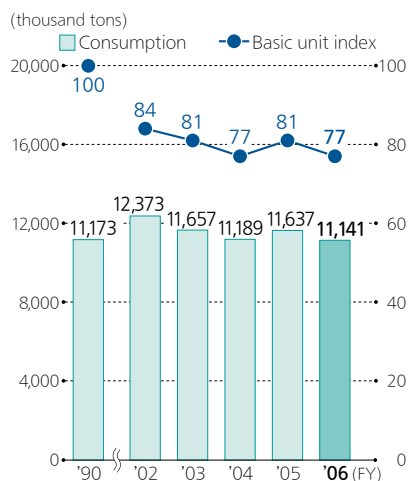
In fiscal year 2005, groundwater at the Wakayama, Tochigi, and Sakata plant sites was analyzed and measurements of substances covered by environmental standards were taken. This was done in light of the history of chemical usage at these locations, and all detected substances were within standards. In fiscal year 2004, dissolution tests and measurements of substances covered by environmental standards were performed on soil at the Kawasaki Plant site and no contamination was detected.

No soil tests or measurements were performed in fiscal year 2006, but measures like pouring a concrete slab to cover an area around the incinerators were taken in preparation for possible accidents and to prevent soil contamination.

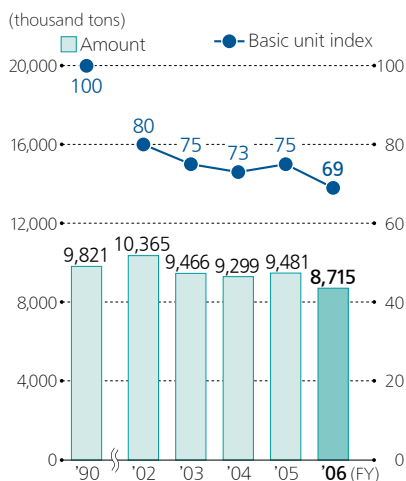
### Measures for biodiversity preservation

Biodiversity is an indispensable structural element of the ecosystem including human beings and plays an important role in maintaining the sustainability of our lives and the

### Trends in Water Consumed

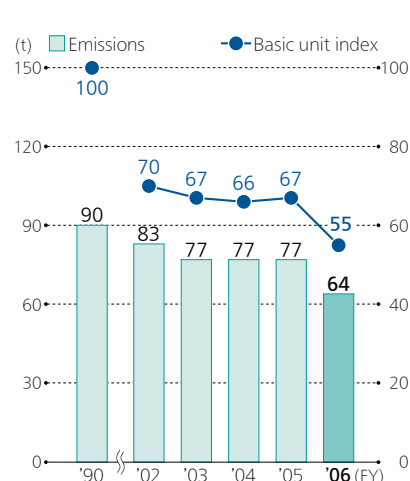


### Trends in Wastewater Amount



\*Due to a change in the calculation method, data for fiscal year 2005 differ from those reported in CSR Report 2006.

### Trends in COD Emissions



natural environment. That said, however, various forms of environmental burden caused by humans have led to a relentless decline in biodiversity. Kao, therefore, is engaged in a host of initiatives that help to preserve biodiversity.

In fiscal year 2006, Kao formally joined the Roundtable on Sustainable Palm Oil (RSPO) (See page 15). Palm oil has gained attention as a sustainable, renewable resource and its growing production has given rise to social and environmental problems like ecosystem destruction, in the form of tropical rain forest logging, and harsh working conditions on plantations. RSPO is an international NGO that aims to solve these problems. Moving forward, Kao continue to consider the importance of the environment from a global perspective and promote sustainable raw material procurement. Kao also supports afforestation and the preservation of community forests through activities like the "Kao Creating Forests for Everyone" program (See page 48) and the "Kao Teacher Fellowship Program" (See page 48), which provides schoolteachers with the opportunities to participate in overseas field research projects on biodiversity.

### Efforts to lower environmental burden after product usage

Wastewater containing laundry detergent and other household products is broken down by microorganisms at wastewater treatment plants and in rivers, and returned to the natural cycle in rivers, lakes, and oceans. Plastics used in containers and packaging materials, on the other hand, are not broken down in the ecosystem, so they are recycled or

incinerated in special facilities. We, therefore, rely on two systems — the ecosystem and man-made processes — to clean and recirculate the wastewater and waste materials resulting from the use of consumer products.

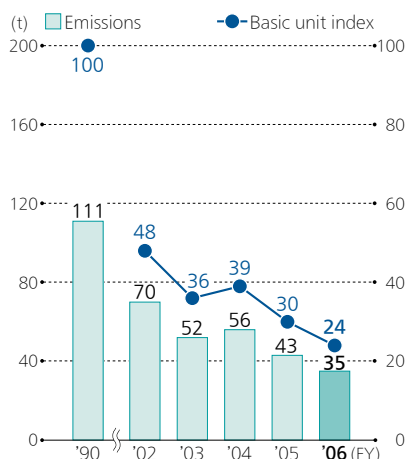
To avoid overloading these systems, Kao, which has made promoting the reduction of environmental burden throughout product lifecycles the basic policy of its environmentally conscious product design, strives to use raw materials that are highly biodegradable and impart minimal impacts on the ecosystem.

Kao also pays close attention to the influence products have on rivers and other aspects of the natural environment after they are used. In that light, we are working with other members of the Environment and Material safety Subcommittee in the Environmental Committee of the Japan Soap and Detergent Association to perform an environmental monitoring study. In this study, we are assessing risks to the ecosystem posed by LAS and three other surfactants subject to the PRTR Law. We take measurements of these surfactants four times a year in the Tama and three other rivers flowing through urban areas.

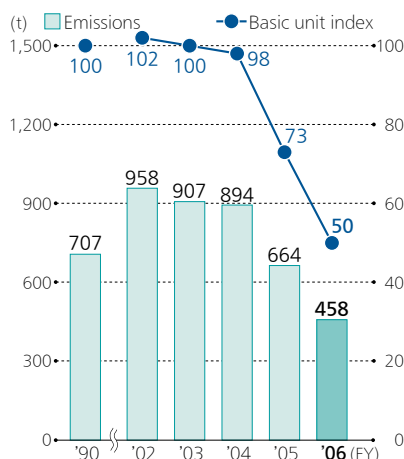
Results for fiscal year 2005 showed that surfactant concentrations were within allowable levels and confirmed that risks to the ecosystem continued to be low, as was indicated in the prior fiscal year (Japan Soap and Detergent Association, *Environmental Annual Report*, Vol. 31 2006 ed.)

HP Japan Soap and Detergent Association  
[http://www.jsda.org/w/e\\_engls](http://www.jsda.org/w/e_engls)

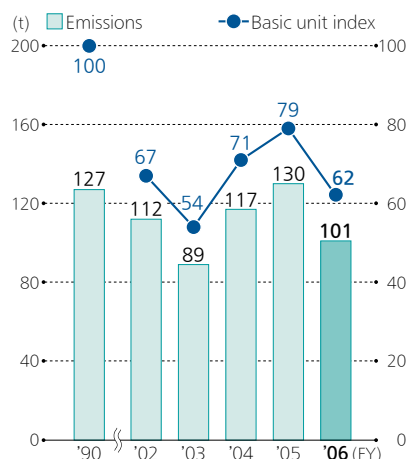
### Trends in SOx Emissions



### Trends in NOx Emissions



### Trends in Soot and Dust Emissions



\*Due to a revision in rounding, data for fiscal year 2002 differ from those reported in CSR Report 2006.

## Kao actively provides information on the results of its scientifically based environmental protection initiatives through various communication activities.

### Various forms of communication focused on the environment

Kao constantly pursues effective communication through a scientific approach, fair and timely information disclosure, and sincere dialogue. Regarding our activities and performance, we provide information via our website and CSR reports, site reports, and booklets like “Everyday Life Information on Environment and Safety.” We place great importance on dialogue, as is demonstrated by our efforts to create opportunities for discussion with consumers such as through factory tours and the activities of our Consumer Communication Center, and the views and desires of stakeholders have been very useful in our daily environmental protection activities.

**HP** Efforts for the environment  
<http://www.kao.co.jp/en/csr/global>

#### Publication of environmental/safety site reports

In fiscal year 2005, Kao began publishing site reports, which provide information on individual plants, for local residents and participants in plant tours. These reports serve as tools for improving understanding of the environmental protection and safety activities pursued by individual plants, and for eliciting opinions from a greater number of individuals. In fiscal year 2006, site reports were issued by all eight domestic plants. The Tokyo Plant, which is located in the Sumida area and is adjacent to a residential area, distributed site reports to local residents.



Environment/safety site reports (Tokyo Plant, Wakayama Plant)

#### Environment/Safety/Disaster Prevention Meeting held

The Tokyo Plant held its Environment/Safety/Disaster Prevention Meeting for local residents in January 2007. The purposes of this meeting were to help local residents better understand measures the Sumida Office has taken to protect the environment, promote safety, and prevent disasters, and to exchange views with local residents. Nineteen leaders of six community associations participated in this meeting.

For its part, Kao reported on its environmental protection activities and provided detailed explanations of its safety activities, comprehensive earthquake disaster prevention drills nighttime emergency drills, and other emergency response activities.



Participants listening to a presentation

#### Participation in the Eco-Products International Fair (Singapore)

Kao participated in the Eco-Products International Fair held October 31 to November 2, 2006 at the Suntec Singapore

International Convention & Exhibition Centre.

Our booth provided information on the history of Kao's environmentally conscious business activities and on various technologies and applications. Examples included refill containers for cleanser and fabric softener products, content concentration and the use of more compact containers, plastics usage reduction through measures like the development of containers with thinner walls, collapsible containers that reduce garbage bulk, and methods for using recycled materials. Having received a large number of opinions and questions from visitors, the majority of whom were housewives, students, and businessmen, we believe our participation in the fair was very meaningful.



Kao booth

#### Environmental education program

The Kashima Plant pursues an environmental education program targeting local junior high school students. The purpose of this effort is to communicate the importance of protecting the global environment to children, on whom the future of society depends.

In fiscal year 2006, the program took place on September 25 and 27 at a junior high school close to the Kashima Plant. On these days, Kao employees who work with environmental matters taught classes under the themes of “global warming”



Students intently listening to an environmental presentation

and “saving energy,” explained to students steps they can take to save energy, and addressed other matters like problems related to asbestos. The Kashima Plant will continue to pursue this program and work to expand environmental education.

#### Promoting forest protection activities through the “Kao Forest” program

In February 2007, Wakayama Prefecture and Kao signed an agreement establishing the “Kao Forest” program to protect 0.7ha of forest in Kimino-cho, Kaiso-gun, Wakayama Prefecture. This is part of the “Corporate Afforestation” project in which Wakayama Prefecture works with local forest cooperatives and other parties to lend sections of forest to companies and other organizations at no cost. Presently, 27 companies are participating in this program. In the “Kao Forest” a tree-planting ceremony was held in April 2007. This ceremony was attended by 100 people, including the Mayor of Kimino-cho, town and prefecture officials, the manager of the Wakayama Plant, and Kao



Tree-planting ceremony

officials. Going forward, Kao will regularly cut grass and undertake other measures as it pursues ongoing efforts to protect this section of forest.

## Methods of Aggregation for FY 2006

- [1] The aggregation methods for FY 2006 comply with the Ministry of the Environment's "Environmental Accounting Guidelines 2005." They also refer to the "Environmental Accounting Guidelines for Chemical Companies (November 2003)" issued by the Japan Chemical Industry Association.
- [2] The accounting scope covers Kao Corporation and its five domestic subsidiaries (Kao Customer Marketing Co., Ltd., Ehime Sanitary Products Co., Ltd., Kao-Quaker Co., Ltd., Kao Professional Service Co., Ltd., and Goldwell Japan Co., Ltd.)
- [3] The accounting period runs from April 1, 2006 to March 31, 2007.

Changes in calculation methods and recalculation of results:

- Figures for energy consumption for production activities (crude oil equivalent, kℓ) were recalculated based on a different calculation method for fiscal years 2005 and earlier, going back to 1990. They, therefore, differ from those reported in CSR Report 2006.
- Greenhouse gas emissions (CO<sub>2</sub> equivalent) were recalculated based on the Calculation and Reporting Manual for Greenhouse Gas Emissions Ver. 1.2) issued by the Ministry of the Environment and the Ministry of Economy, Trade and Industry in February 2007.
- Wastewater figures for fiscal year 2005 differ from those reported in CSR Report 2006 because of a partial revision of the calculation method.

## Environmental Conservation Cost (Categories Corresponding to Business Activities)

(Unit: million yen)

Categories	Key Activity and the Outcome	Investment	Cost* <sup>1</sup>
(1) Business Area Costs		1,147	3,596
Breakdown 1) Pollution Prevention Cost	Air and water pollution prevention	776	1,693
2) Global Environmental Conservation	Energy conservation	37	81
3) Resource Circulation Cost	Resource saving, waste treatment and disposal	334	1,823
(2) Upstream/Downstream Cost	Plant and equipment for environmentally-friendly products, containers, and packaging recycling	927	2,659
(3) Administration Cost	Acquisition and maintenance of ISO certification, environmental publicity, tree planting within work sites	13	866
(4) R&D Cost	Environmentally-friendly R&D	259	2,040
(5) Social Activity Cost	Natural environmental conservation and tree planting activities outside work sites, donations	0	56
(6) Environmental Remediation Cost		—	0
<b>Total</b>		<b>2,345</b>	<b>9,217</b>

\*<sup>1</sup> Expense amounts include depreciation costs.

## Environmental Conservation Benefit

Environmental Performance Indicators (units)	FY2005	FY2006	Change* <sup>2</sup>
<b>Categories</b>			
Related to Resources Input into Business Activities			
Energy consumption of production activity (crude oil equivalent, kℓ)	207,394	205,121	▲2,273
Water consumed (1,000 t)	11,637	11,141	▲496
Related to Waste or Environmental Impact Originating from Business Activities			
Greenhouse gas emissions (CO <sub>2</sub> equivalent: 1,000 t)	476	467	▲9
SOx emissions (t)	43	35	▲8
NOx emissions (t)	664	458	▲206
Wastewater amount (1,000 t)	9,481	8,715	▲766
COD emissions (t)	77	64	▲13
Waste discharged (1,000 t)	30	33	3
Final disposal amount of waste (1,000 t)	0.5	0.3	0
Emissions of chemical substances subject to PRTR Law to the air (t)	4	3	▲1

\*<sup>2</sup> ▲ represents a decline.

## Economic Benefit Associated with Environmental Conservation Activities

(Unit: million yen)

Details of Benefit		Amount* <sup>3</sup>
Revenue from sales of valuable residues	Sales value of valuable resources and fixed assets	187
Cost reduction	Reduction in costs through energy conservation	365
	Reductions in cost through resource saving	2,431
	Reduction in operation costs (maintenance costs, etc., of environmentally-friendly equipment)	190
<b>Total</b>		<b>3,174</b>

- \*<sup>3</sup> The amounts of cost reduction represent annual reduction amounts of the items generated in the respective fiscal year.
- For economic effect, only the amounts from selling valuable resources and fixed assets and the amounts of cost reduction are recorded. So-called "deemed effects," or economic effects based on risk evasion and other assumptions, are not recorded.
  - The Guidelines by the Ministry of the Environment specify that the profit gained from the sale of valuable resources and fixed assets should be recorded. However, we recorded the sales values themselves as it is difficult to calculate the profit accurately.
  - Amounts of cost reductions are recorded only for the relevant fiscal year for the annual reduction amount for items generated during that year. Cost reduction amounts to be generated over multiple years are not included.

## Environmental Conservation Cost (Categories Corresponding to Areas of Application of Environmental Conservation Measures)

(Unit: million yen)

Categories	Details of Measures	Investment	Cost
(1) Cost related to global warming measures	Energy conservation	37	81
(2) Cost related to ozone layer protection measures		0	0
(3) Cost related to air quality conservation measures	Air pollution prevention, prevention of dust pollution, malodor prevention	508	583
(4) Cost related to noise and vibration measures	Prevention of noise	0	10
(5) Cost related to environmental conservation measures for the aquatic, ground, and geologic environments	Prevention of water pollution	268	1,100
(6) Cost related to waste and recycling measures	Resource saving, industrial waste volume reduction, recycling	1,261	4,482
(7) Cost related to measures for reducing chemical risk and emissions	R&D on products and production	259	2,040
(8) Cost related to natural environmental conservation	Natural environmental conservation and tree planting activities outside work sites, donations	0	56
(9) Other costs	Acquisition and maintenance of ISO certification, environmental publicity, tree planting activities within work sites	13	866
<b>Total</b>		<b>2,345</b>	<b>9,217</b>

## Trends Chart for Summary Environmental Accounting Data for the Three Most Recent Periods

Categories		FY 2004	FY 2005	FY 2006
(1) Environmental Conservation Cost	Investment (million yen)	1,987	2,322	2,345
	Cost (million yen)	9,519	9,530	9,217
(2) Environmental Performance Indicators Concerning Environmental Conservation Benefit	Energy consumption of production activity (crude oil equivalent, kℓ)	204,954	207,394	205,121
	Water consumed (1,000 t)	11,189	11,637	11,141
	Greenhouse gas emissions (CO <sub>2</sub> equivalent: 1,000 t)	479	476	467
	SOx emissions (t)	56	43	35
	NOx emissions (t)	894	664	458
	Wastewater amount (1,000 t)	9,299	9,481	8,715
	COD emissions (t)	77	77	64
	Waste discharged (1,000 t)	32	30	33
	Final disposal amount of waste (1,000 t)	2	0.5	0.3
	Emissions of chemical substances subject to PRTR Law to the air (t)	5	4	3
(3) Economic Benefit Associated with Environmental Conservation Activities	Actual benefit (million yen)	2,262	1,675	3,174

## Cross-References between this Report and GRI Guideline Indicators

Vision and Strategy		
1.1	Statement of vision and strategy	P.2-3, 20
1.2	Statement from the CEO	P.2-3
Profile		
Organizational Profile		
2.1	Name of reporting organization	P.4
2.2	Major products and/or services	P.5
2.3	Operational structure	P.4-5
2.4	Description of major divisions, subsidiaries, etc.	P.4-5
2.5	Countries in which the organization's operations are located	P.4-5
2.6	Nature of ownership	P.4-5
2.7	Nature of markets served	P.4-5
2.8	Scale of the reporting organization	P.4-5
2.9	List of stakeholders	P.7
Report Scope		
2.10	Contact person(s) for the report	P.65
2.11	Reporting period for information provided	P.1
2.12	Date of most recent previous report	P.1
2.13	Boundaries of report and any specific limitations on scope	P.1
2.14	Significant changes that have occurred since the previous report	P.1, 16
2.15	Basis for reporting on situations that can significantly affect comparability from period to period and/or between reporting organizations	No important reporting matters
2.16	Explanation of the nature and effect of any re-statements of information provided in earlier reports	No significant changes
Report Profile		
2.17	Decisions to apply GRI principles or protocols in the preparation of the report	Used as reference
2.18	Criteria/definitions used in any accounting for economic, environmental, and social costs and benefits	P.61
2.19	Significant changes from previous years in the measurement methods applied to key economic, environmental, and social information	No significant changes
2.20	Policies and internal practices to enhance and provide assurance about the accuracy, completeness, and reliability	P.64-65
2.21	Policies and current practice with regard to providing independent assurance for the entire report	P.64
2.22	Means by which report users can obtain additional information and reports on the organization's activities	P.61
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3.2	Percentage of the Board of Directors that are independent, non-executive directors	P.18
3.3	Process for determining the expertise board members	P.18
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3.5	Linkage between executive compensation and achievement of the organization's financial and non-financial goals	P.18
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3.10	Approaches to stakeholder consultation	P.7, 32-48
3.11	Type of information generated by stakeholder consultations	P.7, 32-48
Overarching Policies and Management Systems		
3.13	Explanation of whether and how the precautionary approach or principle is addressed by the organization	P.23-29
3.14	Externally developed charters, sets of principles, or other initiatives to which the organization subscribes or endorses	P.2, 20
3.15	Principal membership in association and organizations	—
3.16	Policies and/or systems for managing upstream and downstream impacts	—
3.17	Reporting organization's approach to managing indirect impacts resulting from its activities	—
3.18	Major decisions during the reporting period regarding the location of, or changes in, operations	No significant changes
3.19	Programs and procedures pertaining to performance	P.29, 52
3.20	Status of certification pertaining to management systems	P.29

Economic Performance Indicators		
Customers		
EC1	Net sales	P.4
EC2	Geographic breakdown of markets	P.4
Suppliers		
EC3	Cost of all goods, materials, and services purchased	AR
EC4	Percentage of contracts that were paid	—
Employees		
EC5	Total payroll and benefits broken down by country or region	—
Providers of Capital		
EC6	Dividends to investors	P.42
EC7	Increase/decrease in retained earnings	AR
Public Sector		
EC8	Total sum of all types of taxes paid broken down by country	AR
EC9	Subsidies received broken down by country or region	—
EC10	Donations broken down in terms of cash and in-kind donations per type of group	—
Environmental Performance Indicators		
Materials		
EN1	Total materials used, other than water, by type	P.50-51
EN2	Percentage of materials used that are wastes from sources external to the reporting organization	P.56
Energy		
EN3	Direct energy use segmented by primary source	P.50-51, 53
EN4	Indirect energy use	P.50-51
Water		
EN5	Total water use	P.50-51, 58
Biodiversity		
EN6	Location and size of land owned, leased, or managed in biodiversity-rich habitats	Not applicable
EN7	Description of the major impacts on biodiversity associated with business activities	—
Emission, Effluents, and Waste		
EN8	Greenhouse gases	P.50-51, 53
EN9	Ozone-depleting substances	P.55, Web
EN10	NO <sub>x</sub> , SO <sub>x</sub> , and other significant air emissions by type	P.50-51, 59
EN11	Total amount of waste by type	P.56, Web
EN12	Discharges to water by type	—
EN13	Spills of chemicals, oils, and fuels	P.58 (No significant spills)
Products and Services		
EN14	Significant environmental impacts of principal products and services	—
EN15	Products that are reclaimable at the end of the products' useful life	P.57
Compliance		
EN16	Non-compliance with environmental laws and regulations	P.58
EN17	Renewable energy	—
Transport		
EN34	Environmental impacts of transportation used for logistical purposes	P.50-51, 54
Overall		
EN35	Total environmental expenditures by type	P.61

Social Performance Indicators		
Employment		
LA1	Breakdown of workforce	P.37
LA2	Net employment creation and turnover	P.37
LA12	Employee benefits beyond those legally mandated	P.37
Labor/Management Relations		
LA3	Breakdown of trade unions, etc.	—
LA4	Policies and procedures involving information, consultation, and negotiation with employees over changes in the reporting organization's operations	—
Health and Safety		
LA5	Practices on recording and notification of occupational accidents and diseases	P.40
LA6	Description of formal joint health and safety committees	P.7
LA7	Standard injury, lost day, and absentee rates and number of work-related fatalities	—
LA8	Description of policies or programs on HIV/AIDS	—
Training and Development		
LA9	Hours of training by employee category	P.36
LA16	Description of programs to support the continued employability of employees and to manage career endings	P.39
LA17	Specific policies and programs for skills management or for lifelong learning	P.36
Diversity and Opportunity		
LA10	Equal opportunity policies or programs	P.37-38
LA11	Composition of senior management and corporate governance bodies	—
Human Rights: Strategy and Management		
HR1	Policies to deal with human rights issues relevant to operations	P.21, 37
HR2	Consideration of human rights impacts as part of investment and procurement decisions	P.41
HR3	Policies and procedures to address human rights performance within the supply chain	P.41
HR8	Employee training on policies and practices concerning all aspects of human rights relevant to operations	P.38
Non-discrimination		
HR4	Policies and procedures to prevent all forms of discrimination in operations	P.21, 37
Freedom of Association and Collective Bargaining		
HR5	Freedom of association	P.20
Child Labor		
HR6	Policies excluding child labor	P.20-21
Forced and Compulsory Labor		
HR7	Policies to prevent forced or compulsory labor	P.20-21
Disciplinary Practices		
HR9	Appeal practices	P.21
HR10	Non-retaliation policy	P.21
Community		
SO1	Policies to manage impacts on communities	—
SO4	Award received relevant to social, ethical, and environmental performance	P.30
Bribery and Corruption		
SO2	Policies and practices to address bribery and corruption	P.21
Political Contributions		
SO3	Policies and procedures for controlling political lobbying and contributions	P.21
SO5	Money paid to fund political parties or their candidates	Not applicable
Competition and Pricing		
SO6	Anti-trust and monopoly regulations	Not applicable
SO7	Preventing anti-competitive behavior	P.21
Customer Health and Safety		
PR1	Preserving customer health and safety	P.26-27
PR4	Non-compliance with regulations concerning customer health and safety	Not applicable
PR5	Number of complaints upheld by regulatory bodies	—
PR6	Voluntary code compliance, product labels or awards received	Not applicable
Products and Services		
PR2	Products information and labeling	P.25
PR7	Non-compliance with regulations concerning product information and labeling	Not applicable
PR8	Customer satisfaction	P.33
Advertising		
PR9	Standards related to advertising	P.21
Respect for privacy		
PR3	Protection of consumer privacy	P.22

This cross-reference table specifies the pages of the report that are related to respective GRI Guideline requirements and does not guarantee compliance.

The characters in green and "AR" represent the corresponding sections of the ten principles of the Global Compact and matters dealt with in the annual report (AR), respectively.



Kao has positioned its CSR Report as an information disclosure tool responding to the interest stakeholders take in Kao, and we carefully consider the opinions and comments we receive from inside and outside the company in enhancing the quality of information carried in our CSR reports. We raise the level of our CSR activities by applying in daily activities what we learn through these opinions and comments, and, therefore, place great value on CSR reports as a communication tool for deepening mutual understanding.

Based on this perspective, Kao garners employee opinions through means including surveys of those who have read the

CSR report, CSR report reading meetings, and CSR seminars (See page 20).

To garner the opinions of parties outside the company, we request responses to our FAX-based survey and have implemented a system that allows people to easily send us their opinions via our website. Additionally, we hold face-to-face gatherings to discuss themes such as the environment, safety, product quality, and communication with consumers.

Moving into the future, Kao will continue to reflect the opinions it receives on both its CSR activities and reports, and, thereby, further enhance communications with its stakeholders.

## Opinions and Responses to Kao's CSR Report 2006

### Opinions and responses received via the FAX survey included in the report

(As of the end of May 2007: Responses = 50)

Seventy percent of respondents indicated that the report was "easy to understand" and "very informative," and 75% said that its length was "just right."

#### Sections that were particularly interesting or impressive (Multiple responses permitted)

1. Message from the President & CEO	28%
2. Relationships with Employees	22%
3. Initiatives for Ensuring Product Safety	18%
3. System for CSR Promotion	18%
3. Corporate Citizenship Activities	18%
3. Relationship with Communities	18%

#### Opinions and responses received

- As a report for those reading from an expert perspective, it is very good, but it is too detailed for ordinary people.
- The report permits a full understanding of the thoroughness of the systems of a company with deep relationships with consumers.
- It is now very important for companies to have relationships with local communities. I want to consider this point when choosing products in a supermarket.
- Concerning the nurturing of the next generation, I would like to hear more about what to do now, based on considerations of what conditions will be like 10 or 20 years into the future.
- I have a favorable impression based on the description of measures taken in response to negative circumstances, like risks related to chemical substances and the use of large volumes of containers and packaging materials. It would be good if there were coverage (including concrete figures) of CSR initiatives cognizant of the ecosystem.

#### Improvements

With this report, we have made several changes based on comments about last year's report. Examples include a revision of the chapter structure, which was cited as difficult to understand, the use of titles that are more easily searchable, and placement of terminology explanations in more easily accessible locations. All of these changes were

### Opinions and responses received via Kao's website

(As of the end of May 2007: Responses = 61)

Approximately eighty percent of respondents were ordinary consumers. Two-thirds of respondents were in their 20s or 30s.


Areas receiving the greatest numbers of responses were: Environmental Activities (31%), Social Activities (23%), and initiatives supporting safety (21%).

#### Opinions and responses received

- Report is difficult for ordinary people to understand. I would like the text to be made easier to understand.
- I would like Kao to not only be very thorough regarding CSR that should be addressed through its business, but to also engage in an ongoing dialogue with society, continuously work to motivate employees, and contribute to society as a more broad-minded company.
- I select cosmetics and other products based on the manufacturer's environmental consciousness and on whether the manufacturer conducts animal testing. I now know that Kao is making positive efforts in both areas. In the future, I would like Kao to manufacture more products that have not been animal-tested.
- Environmentally conscious company activities are now indispensable, and I would like Kao to be more proactive in this sense. However, I think there are probably many consumers who are unfamiliar with Kao's environmental initiatives.
- The activities of Kao Peony, which provides employment for intellectually disabled people, are very meaningful. I look forward to seeing these activities further developed.
- The information is comprehensive. And, opinion-garnering efforts like this tell me this company is very serious, but I would like for Kao to come up with content that is more interesting for readers.

made to improve report readability.

Moving ahead, Kao will continue to listen to stakeholders' opinions carefully and improve its CSR activities step-by-step.

 CSR Report  
<http://www.kao.co.jp/en/csr/report/>

(TRANSLATION)

Independent Review Report

June 20, 2007

Mr. Motoki Ozaki,  
President and CEO, Kao Corporation

Tohmatsu Environmental Research Institute Ltd.  
Chief Executive Officer Komuro, Masamitsu

1. Scope of the Review

We have reviewed the "CSR Report 2007" ("Report") prepared by Kao Corporation ("Company"). The purpose of our review was to provide limited assurance from an independent practitioner about whether the material quantitative environmental information for the period from April 1, 2006 to March 31, 2007 included in the Report was accurately measured and calculated, referring to the Environmental Reporting Guidelines -Fiscal Year 2003 version (issued by the Japanese Ministry of the Environment) and GRI Sustainability Reporting Guidelines (2002), in accordance with calculation methods adopted by the Company.

2. Responsibility of the Management

The Report is the responsibility of the Company's management. Our responsibility is to provide our limited assurance with respect to the review performed on the Report from an independent practitioner.

3. Summary of Review

To obtain an adequate and valid standard of basis for providing limited assurance with respect to our conclusions, we performed our review with reference to the International Standard on Assurance Engagements (ISAE) 3000 (issued by the International Federation of Accountants in December 2003) and the Proposed Environmental Report Review Standard (issued by the Japanese Ministry of Environment in March 2004).

The review procedures performed for the material quantitative environmental information for the period from April 1, 2006 to March 31, 2007 included in the Report consisted of; 1) agreeing information to summary tables and supporting documents on a sample basis; 2) interviewing the responsible personnel and the persons in charge; 3) reviewing and agreeing information to the relevant minutes, the Company's regulations, and ISO related documents and so on; 4) site visits; and 5) comparing information with other available supporting internal and external materials.

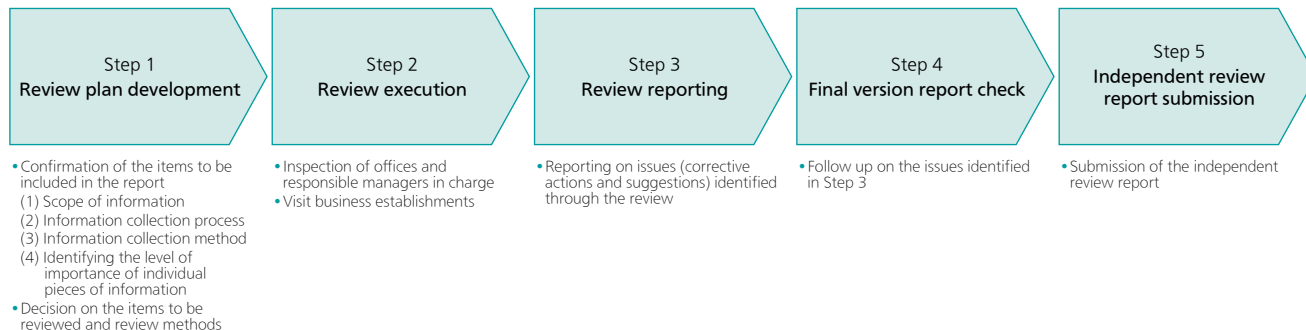
4. Conclusions

On the basis of the review procedures described in the preceding paragraph, nothing has come to our attention that caused us to believe the material quantitative environmental information for the period from April 1, 2006 to March 31, 2007 included in the Report was not accurately measured or calculated, referring to the Environmental Reporting Guidelines -Fiscal Year 2003 version (issued by the Japanese Ministry of the Environment) and GRI Sustainability Reporting Guidelines (2002), in accordance with calculation methods adopted by the Company.

5. Special Interests

There are no interests between the Company and Tohmatsu Environmental Research Institute Ltd. or its engagement personnel, requiring disclosure referred to the provisions of the Certified Public Accountants Law of Japan.

## Procedure for Preparation of the Independent Review Report



The auditors visited the following establishments during the review: Kayabacho Head Office, Wakayama Plant, Ehime Sanitary Products Co., Ltd.. Visits to the above establishments were carried out in accordance with the planned schedule. As for offices and plants that the auditors could not visit, the auditors reviewed and confirmed the relevant information at the Kayabacho Head Office.



### Please forward any inquiries to

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The CSR Report is also available at Kao's Web site.  
<http://www.kao.co.jp/en/csr/report>  
Issued: August 2007

### Environmental Consideration of This Report

Our report uses FSC forest-certified paper, which includes materials shipped from forests that are properly managed, and soy oil ink, which reduces the occurrence of VOCs (volatile organic compounds). For printing, a waterless printing method that does not produce effluents that include harmful substances has been adopted.



Kao Corporation

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