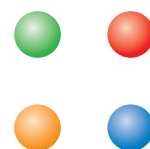




CSR Report 2006

2005.04.01 – 2006.03.31

Kao Corporation



Kao's CSR is the fulfillment of The Kao Way.

As to the corporate philosophy that forms the basis of our business activities, Kao reviewed its previous "Kao Management Principles" from a global point of view. In October 2004, we formulated The "Kao Way" to manifest Kao's unique corporate culture and its spirit of enterprise. For Kao, Corporate Social Responsibility (CSR) is to implement *Yoki-Monozukuri* based on The Kao Way and to strive for the satisfaction and enrichment of the lives of people globally.

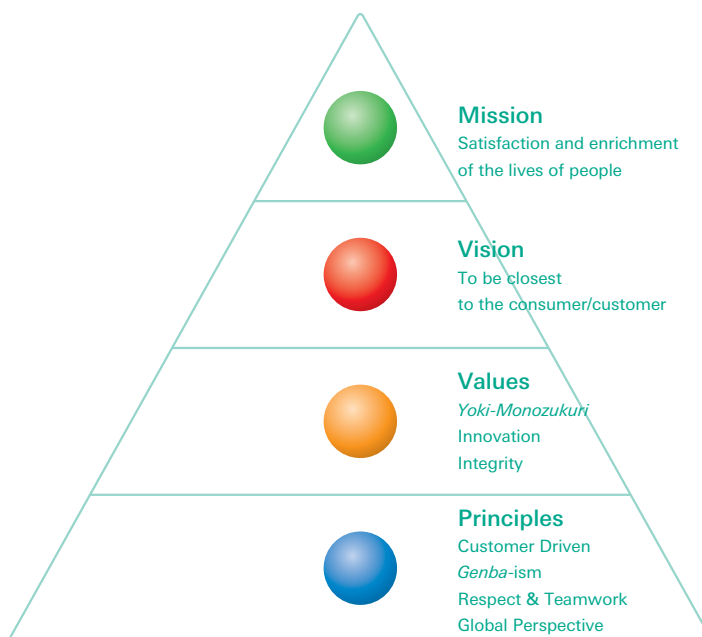
Yoki-Monozukuri

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."

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.

The Kao Way



Kao's Approach to CSR

- Kao's mission is "to strive for the wholehearted satisfaction and enrichment of the lives of people globally." In carrying out this mission, Kao strives to globally promote CSR activities and thereby contribute to the sustainable development of society.
- In implementing *Yoki-Monozukuri*, Kao evaluates the economic, environmental, and social elements at each stage of its operations, including product development, procurement, production, distribution, use, and disposal from the viewpoint of the sustainable development of society, and always seeks to make further improvements.
- To improve the fairness and transparency of corporate activities, Kao discloses accurate and relevant information promptly and fairly, and promotes dialogue with a range of stakeholders, including consumers and customers, to monitor its operations from the viewpoint of society.
- Kao conducts CSR Activities based on ethics and compliance with law.

For details on The Kao Way, refer to page 53 and our Web site at <http://www.kao.co.jp/en/company/kaoway/>

●Editorial Policy

This report introduces Kao's operation from the perspective of Corporate Social Responsibility (CSR), with a focus on activities in Japan during fiscal year 2005. We plan to use the report as a communication tool to promote dialogue with a variety of stakeholders.

In 1998, Kao started issuing the Environment, Safety and Health Report in an effort to enhance disclosure. Last year, the title of the report was changed to the CSR Report, and we now incorporate more information on our social performance.

This report is organized into chapters on "Management Systems," "Social Activities," and "Environmental Activities," taking into account of the differing interests and concerns of a wide range of stakeholders. The report also offers Main CSR Topics in FY 2005 in an easy-to-understand format.

●Scope of Reporting

Organization covered:

Basically, Kao's domestic group companies (See page 52.) are covered. When the organizations other than the above are reported, it is clearly noted in the text. Please note that Kanebo Cosmetics Inc. is not covered in this report.

Period covered:

Performance data covers fiscal year 2005 (April 1, 2005 to March 31, 2006). However, activities in fiscal year 2006 are partially covered.

Independent Review:

As in our previous reports since 2003, CSR Report 2006 has been reviewed by a third party. This year, the report was reviewed by the Tohatsu Environmental Research Institute Ltd.

Activities covered:

The Report covers CSR activities in relation to business operations described on pages 4 and 52.

*Detailed data on economic performance is available in our Annual Report 2006.

Issuing period:

Issue date of the previous report: August 2005
Next scheduled issue of the report: August 2007

Guidelines referenced:

- GRI 2002 Sustainability Reporting Guidelines
- Environmental Reporting Guidelines (2003) by the Ministry of the Environment of Japan
- Environmental Accounting Guidelines (2005) by the Ministry of the Environment of Japan

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Aiming to be an attractive company that can share joy with all stakeholders through CSR initiatives

Q What status do you give to CSR initiatives in Kao's business operations?

We, at Kao Group, are aiming to achieve growth and development in our business operations and to be a company respected and trusted by all stakeholders as a responsible corporate citizen. CSR is an essential viewpoint to achieve these objectives.

Kao's CSR activities are based on our mission of striving for the wholehearted satisfaction and enrichment of the lives of people through *Yoki-Monozukuri*, which is at the core of our business operations. In addition, it is also important to review and assess our operation from the viewpoints of our varied stakeholders and to continuously improve and innovate the means and processes through which we conduct

Q What is the basic framework for CSR activities?

The fulfillment of The Kao Way, our corporate philosophy, is most important. The Kao Way stipulates, as its 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."

The phrase, "closest to the consumer/customer," represents our ideal of being a company literally closest to our consumers and customers, that knows them better than anybody else and wins the greatest trust from them. This is exactly the vision of Kao's CSR.

Kao's basic stance on CSR activities is to conduct business toward this vision in accordance with the Kao's Business Conduct Guidelines, which specify guidelines for Kao's corporate activities and for the conduct of individual members.

In 2005, Kao participated in the United Nation's Global Compact. For fiscal 2006, we will continue to fulfill the responsibilities as a participating company.

Q What relationship do Kao's CSR activities have with its corporate culture?

According to the basic concept of CSR, a company must evenly balance the interests of all stakeholders, including consumers, customers, employees, business partners, local communities, and shareholders, from economic, social, and environmental aspects. To this end, a company must be open to society, continue dialogue with stakeholders and incorporate stakeholder feedback into efforts to improve management.

Kao's mission is to strive for the wholehearted satisfaction and enrichment of the lives of people through *Yoki-Monozukuri*. We regard the implementation of The Kao Way and the promotion of CSR as important for creating a corporate culture to achieve our corporate mission. We therefore see CSR activities as a major driving force in our management.

Q What are future priority initiatives?

Firstly from the economic aspect, it is becoming important issue to shift to, and secure sustainable resources for manufacturing our products from the business continuity perspective. To manufacture Kao's products we are using such materials as plant-derived oil, petroleum, and pulp. There are growing concerns worldwide about possible depletion of fossil fuels, and loss of biodiversity from harvesting specific factories as well as global working conditions. It is important to take preemptive measures so that such problems will not be restraining factors in our operations in 10 or 20 years from now.

From the social aspect, we will make full use of diverse groups of human resources. We aim at creating a workplace where personnel with a variety of backgrounds can find their work rewarding, from the viewpoint of equal partnership and a work and life balance. It is part of such efforts to establish Kao Peony Co., Ltd. for the purpose of providing job opportunity to the intellectually challenged. We will also promote social contribution activities proactively and globally to promote the nurturing of the next generations.

From the environmental aspect, we think that Kao has a role to play in society in light of the fact that Kao uses chemical substances in its products and a great deal of containers and packaging. As to chemical substances, we already operate an original chemical substance control system using a tool called "Master Index" in our group companies. We will apply the system also to our entire supply chain. As to containers and packaging, we should make a significant contribution to the realization of a recycling-oriented society with the 3R approach (Reduce, Reuse, and Recycle). Furthermore, it is a part of corporate responsibility to take measures to prevent global warming as a responsible corporate citizen.

Q What do you think as important in promoting CSR?

I think that it is most important to raise all members' awareness. We distributed copies of the CSR Report 2005 to approximately 17,000 members of Kao group companies in and outside of Japan. We then conducted a survey on the members asking for their impressions of the report. We also held meetings to read the report with members. I think that our members do not necessarily perform their tasks while always paying attention to the wide-ranging activities of the entire organization. However, I realized that members became even more proud of the company and have higher levels of motivation through learning about the company's objectives in such an opportunity.

In order for Kao to promote CSR activities from now on, I believe that it is an important responsibility for top executives to educate members to have a deeper understanding of CSR, to motivate them, and to establish a corporate culture and mechanisms that help members find joy in their work through fulfilling their CSR responsibilities.

Since I assumed the presidency, I have called on members to work vigorously, with a slogan of "A company sharing joy with its customers."

CSR is an initiative to create empathy with a variety of stakeholders. I aspire to make Kao Corporation an attractive company that can share joy with the consumer and customer.

August 2006



Motoki Ozaki
President and CEO
Kao Corporation



Engaging in a wide range of business activities on a global scale

Based on the belief that *Yoki-Monozukuri* is the implementation of CSR, Kao is engaged in business operations in wide-ranging fields across the world.

Since its foundation in 1887, Kao has always made it a top priority to contribute to society through *Yoki-Monozukuri*, which is the essence of our business activities. Beginning with *Kao Soap*, our products range from consumer products essential to daily life, such as detergents, shampoos, napkins, and diapers, through prestige cosmetics for women who pursue beauty, to chemical products that take into account not only performance but also the environment. Since the launch of *Econa* cooking oil in 1999, we have launched products for a healthy life one after another. Kao's global production and sales bases manufacture and sell products catering to the unique needs of diverse local communities. Kao delivers products indispensable for daily life throughout the world.

Company Outline (As of March 31, 2006)

(For details, [See page 52.](#))

Company name: Kao Corporation

Address: 14-10, Nihonbashi Kayabacho 1-chome, Chuo-ku, Tokyo 103-8210 Japan

Founded: June 1887

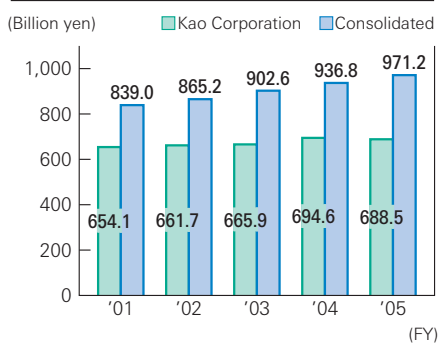
Incorporated: May 1940

Paid-in capital: 85.4 billion yen

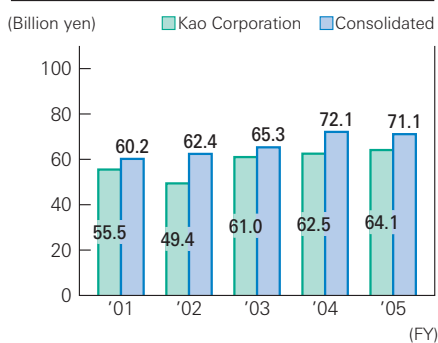
Employees: 5,652 (Number of employees in Kao Group consolidated companies: 19,356)

Representative: Motoki Ozaki, President and CEO

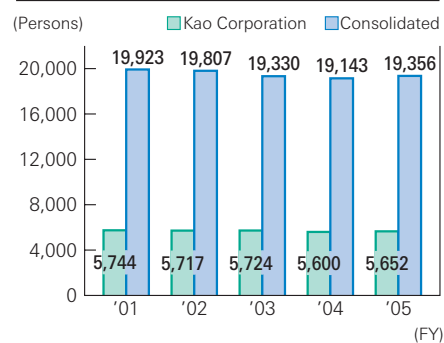
Net Sales



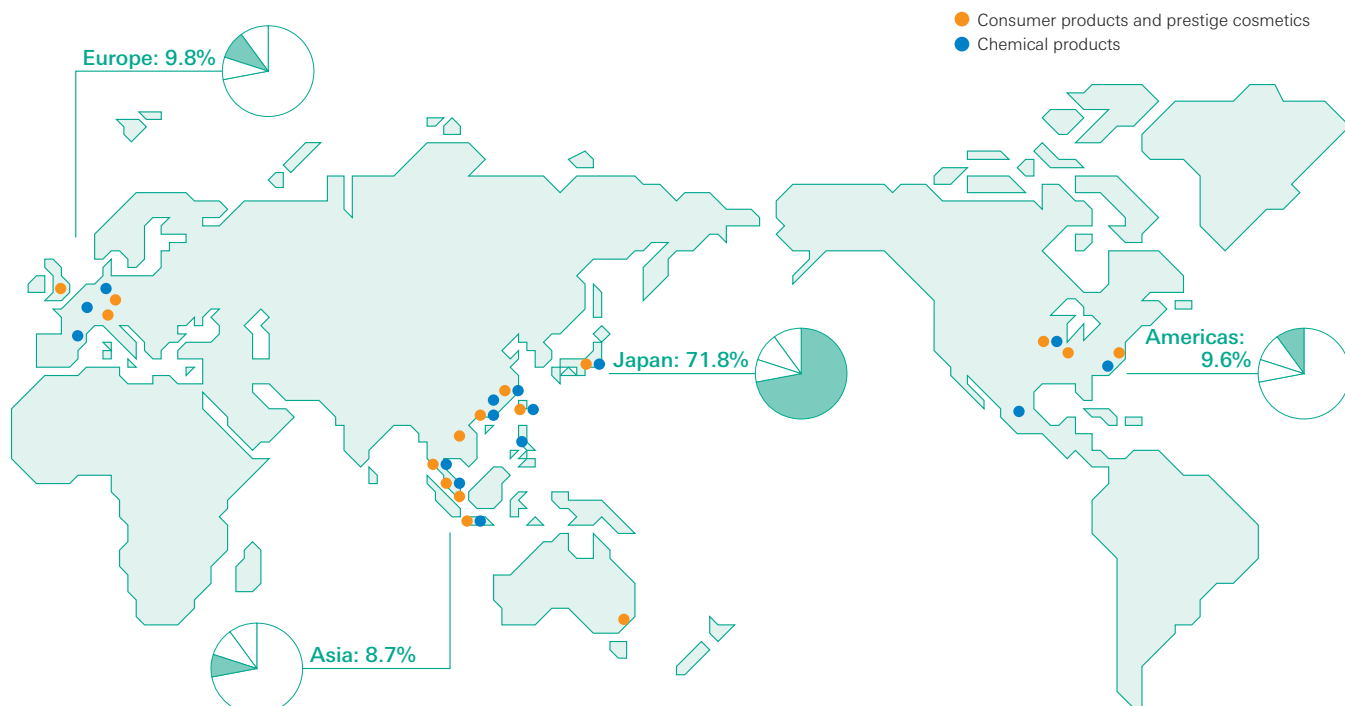
Net Income



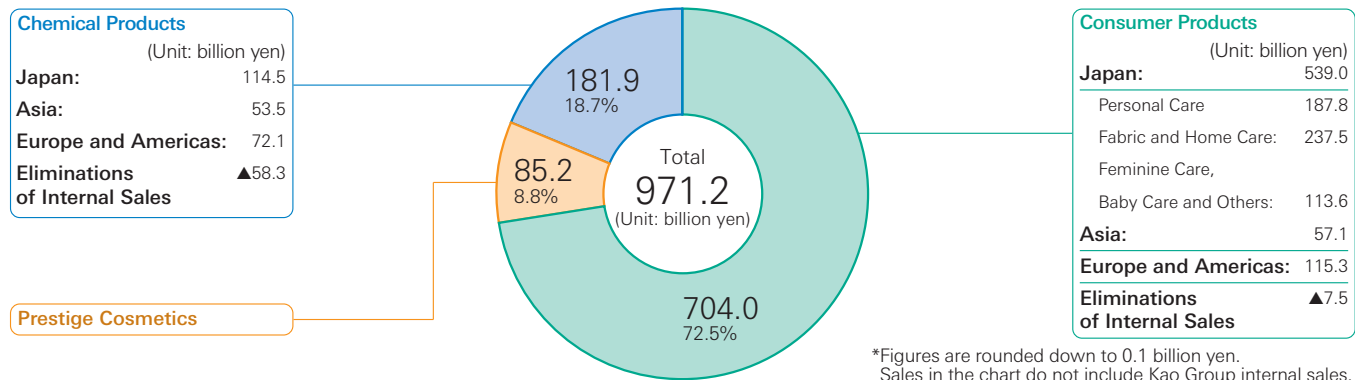
Number of Employees



Global Operations and Breakdown of Net Sales by Region (Fiscal 2005)



Breakdown of Consolidated Sales (Fiscal 2005)



Consumer Products

Every launch of a new product has contributed to the further satisfaction and enrichment of the lives of consumers. Kao is still developing and manufacturing products to deliver cleanliness, beauty, and health for everyday.



Personal Care

Facial care products/Body care products/Hair care products/Bath additives/Oral care products



Fabric and Home Care

Laundry products/Kitchen cleaners/Household cleaners



Feminine and Baby Care

Sanitary napkins/Disposable diapers/Nursing care products/Hygiene care products



Health Care (Functional Food)

Cooking oil/Dressing/Mayonnaise/Drink



Products sold in Asia



Products sold in Europe and Americas



Kao also produces and sells professional-use products

Prestige Cosmetics

In order for women to lead a lively life everyday, Kao offers products that enhance their beauty.



Chemical Products

Kao also operates as a chemical products manufacturer. Based on fats and oil products, Kao provides its products in wide-ranging industrial fields. We produce a host of products, such as de-inking agents used in recycling used paper, and cleaner alternatives to CFCs, that in themselves contribute to the environment and to safety.



Kao meets its social responsibilities through its business activities.

To enrich the lives of people, Kao continues its efforts to develop products that help to keep their lives “clean, beautiful, and healthy.”

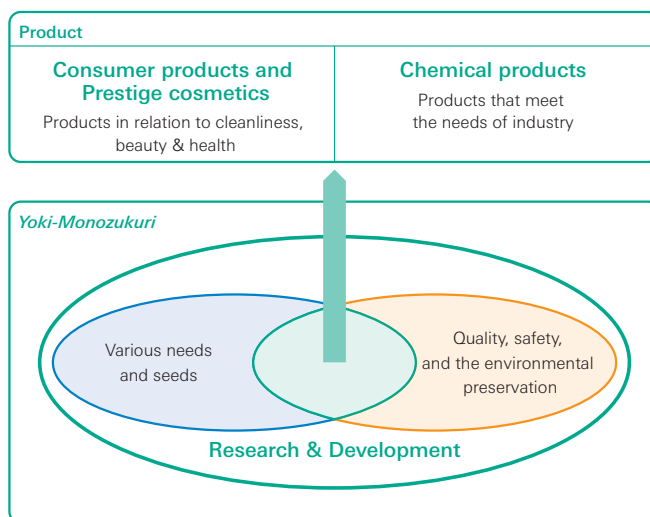
Yoki-Monozukuri—striving to satisfy and enrich the lives of people

Kao wholeheartedly holds up *Yoki-Monozukuri* in developing and manufacturing products as its corporate mission. Through *Yoki-Monozukuri*, we create products that are useful in keeping consumers’ “clean, beautiful, and healthy” lives. Thereby, we contribute to realizing the enriched lives of people throughout the world as our social responsibility.

We also conduct daily business operations based on the belief that contribution through our products helps us to win the support and trust of all stakeholders and facilitates the sustainable development of society.

We believe that we can create the products that can truly contribute to society by integrating the various needs of consumers and customers with Kao’s unique technological seeds and by considering for quality, safety, and the environment.

Yoki-Monozukuri and Research & Development



Fiscal 2005 CSR activities

Adapting to consumers’ lifestyles and habits in each country

From a global perspective, and by directing our attention to the actual lifestyles in respective countries, we are striving to develop best fitting products for each country. For example, laundry is hand-washed in many households in Thailand, causing a significant household burden. Based on this fact, Kao developed a hand-wash detergent, *Attack Easy*, in 2005. This detergent not only washes well but also lessens the work of hand-washing. This product was developed based on our desire to reduce the burden of housekeeping chores as much as we could.



proposal to cope with new lifestyles by coming up with a daily health care product for the people of today.

Contributing to a reduction in environmental burdens

Kao has consistently made efforts to produce and offer products that have less impact on the environment.

In March 2006, a manufacturing process for functional composite powders using supercritical carbon dioxide was recognized as a part of efforts to promote “Green & Sustainable Chemistry”* and it was awarded the fiscal 2005 technology prize by the Society of Chemical Engineers, Japan. This manufacturing technology is mainly used for base makeup cosmetic products. It enables to manufacture the product in an environment-friendly and safe process because no organic solvent is required.



* Green & Sustainable Chemistry: Chemical technology to realize “the health and safety of people and the environmental preservation” and “resource and energy saving” throughout the entire lifecycle of products-including product design, raw material selection, and manufacturing methods.

Developing products that propose a new lifestyle

With changes in the living environment resulting from the wider introduction of office automation equipment and air conditioners, more and more people are complaining about minor ailments, such as low back pains, stiff necks, gastrointestinal problems, and fatigue. Kao focused attention on “thermatology” in response to such physical ailments. Building on its research, Kao released its *Megurhythm Steam Thermo Power Pad* in October 2005. In this way, we made a



Research and development efforts to bring forth the products truly necessary for society

Research and development (R&D) is at the heart of *Yoki-Monozukuri*.

R&D involves two types of activities. First is product development research to design a product and put it into practical use based on consumers' needs. Second is fundamental research to clarify useful mechanisms to work in our products. By integrating two kinds of research activities, Kao strives to develop truly innovative products.

In the product development research, we are engaged in specific product design and application of our research findings based on thorough understanding of consumers' needs. In the fundamental research, which plays a key role in product development, we endeavor to pursue the "truth behind phenomena" by utilizing advanced sciences and technologies in various fields.

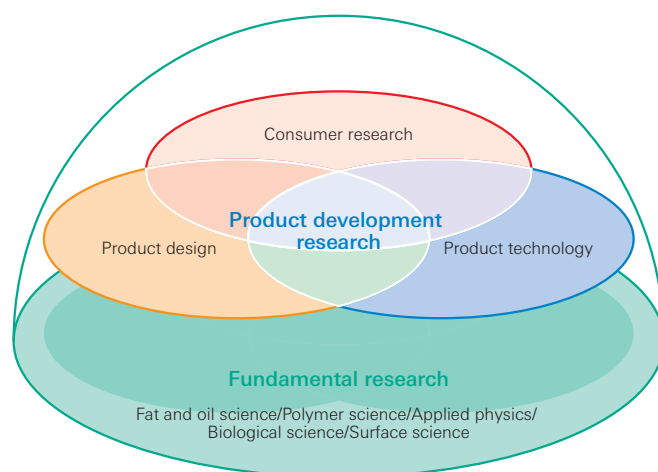
Through these research efforts, Kao aims to develop truly valuable products to indeed make people's lives "clean, beautiful, and healthy."

Matrix management of R&D

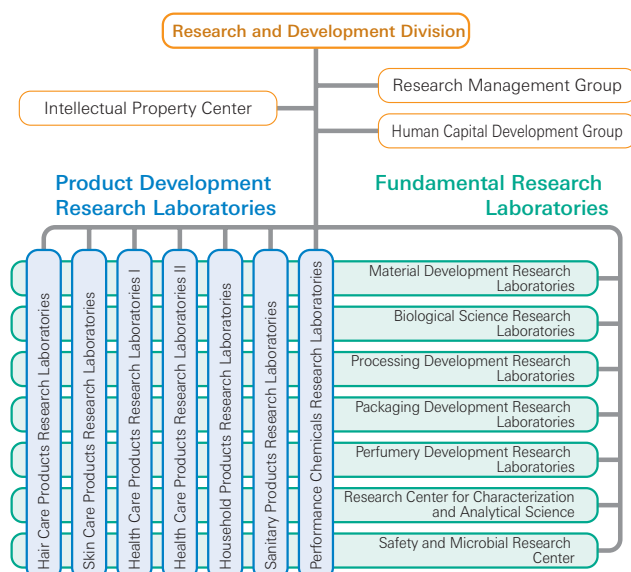
The Product Development Research Laboratories and the Fundamental Research Laboratories are unified as R&D Division. These two research functions cooperate and flexibly form collaborative projects in accordance with specific research subjects. Through such matrix management, expertise in each field can be cross-functionally utilized in a dynamic and flexible

way. This integration facilitates the speedier implementation of our research and development projects.

Integration of Diversified Research



Research and Development Organization



Column

Kao's R&D activities and CSR

The spirit of R&D Division is the untiring challenge of *Yoki-Monozukuri*, which forms the basis of Kao's corporate culture. We strive to create innovative values from the viewpoint of what is best for consumers and customers. To precisely realize greater values for consumers and customers, it is necessary to deepen core fundamental technologies to establish world-class applied technologies. In addition, as one of the Kao's important fundamental technologies, we aim to develop the most advanced technologies in environmental preservation activities. Kao is committed to reduction of the environmental burden and recycling of resources through proposing environmentally-conscious products and services that are truly useful for society.



Toshiharu Numata
President
Global R&D

A woman with dark hair, wearing a white button-down shirt and a black and white patterned skirt, is standing in a store aisle. She is reaching out with her right hand to touch a white bottle of product on a shelf. The shelves are stocked with various personal care products, including bottles of shampoo and body wash, many of which are white or light-colored. The background is slightly blurred, showing more shelves and products.

Feature Reports

Commitment to Safety

As a manufacturer, Kao gives the highest consideration to quality, safety, and environmental impact at every stage of production. We pay due attention to people, local communities, and the natural environment by strictly enforcing chemical substances and other management systems.

Comprehensive approach to quality, safety, and the environment

As a manufacturer of daily necessities, it is a top priority issue for Kao to ensure safety in its corporate activities. To ensure that the highest consideration is given to quality, safety, and the environment at every stage of production, it is necessary to control and reduce the occurrence of various possible risks throughout our business operations. At the same time, it is necessary to minimize damage in the event that a risk becomes real.

Both consumer and chemical products are made of chemical substances. It is extremely important to fully understand the properties of chemical substances and legal standards governing these substances, and to know possible impacts on human health and the environment. It is also essential to make appropriate selections of such substances and to manage them carefully. To this end, Kao enforces integrated, centralized management of chemical substances by means of a chemical substance management system so that we can trace the main substances (traceability) as well as by-product materials.

Kao has also established supervising divisions to carry out quality and environmental tasks in response to critical situations.

To prepare for emergencies, we have clarified, in our Risk Management Policy, priorities of risk management, and responses. We place maximum priority on the lives of all persons—customers, business partners, local residents, and employees. We also place a high priority on environmental conservation and continuation of operations.

- Product safety: [See page 10.](#)
- Safety of employees and local residents: [See page 12.](#)
- Safety of the global environment: [See page 13.](#)

Comprehensively managing chemical substances to give due consideration to quality, safety, and the environment

Kao ensures safety and security from all aspects by comprehensively managing chemical substances to address this important issue.

Comprehensive Management for Chemical Substances

Kao's business ranges widely from chemical materials to products for home use for general consumers and sells several thousand product items and uses more than 10,000 types of raw materials. Pursuit of safety and relief on the products to be delivered to consumers is an important task for a manufacturer.

As one of the tools to fulfill these responsibilities, in 2001 Kao developed its own Comprehensive Management System for Chemical substances. The system utilizes a Master Index, which is a system of chemical substance identification codes unified within the Kao group, as a key data item. In this Management System, Kao's products are registered by raw material and ingredient. The System provides prompt information on which raw materials, and related quality, safety, and legal information, are used in each product. It is easily possible to check all the materials and ingredients of a product, as well as the product's safety, regulatory compliance, and internal management standards.

The information stored in the system is shared by the Procurement, Research & Development, Production, and Quality Assurance divisions. We proceed with development and design, while confirming which raw materials should be used to make a product with higher levels of quality and safety that have less impact on the environment, from the early stages of development and product design. This system enhances traceability, from the procurement of materials to production, and serves as the backbone of Kao's *Yoki-Monozukuri*. The system makes it easy to sum up amount of chemical substances subject to the PRTR law and the data is also incorporated in "Kanchan," Kao's environmental and safety database management system.

Currently, a system to automatically sum up amounts of chemical

substances handled is under development as a part of the Comprehensive Management System for Chemical Substances. In addition to the already monitored chemical substances subject to the PRTR law, the new system will count PRTR materials designated by the Japan Chemical Industry Association (JCIA), volatile organic compounds (VOC), and poisonous & deleterious substances. We will place more materials under control to enhance our management of chemical substances.

Column

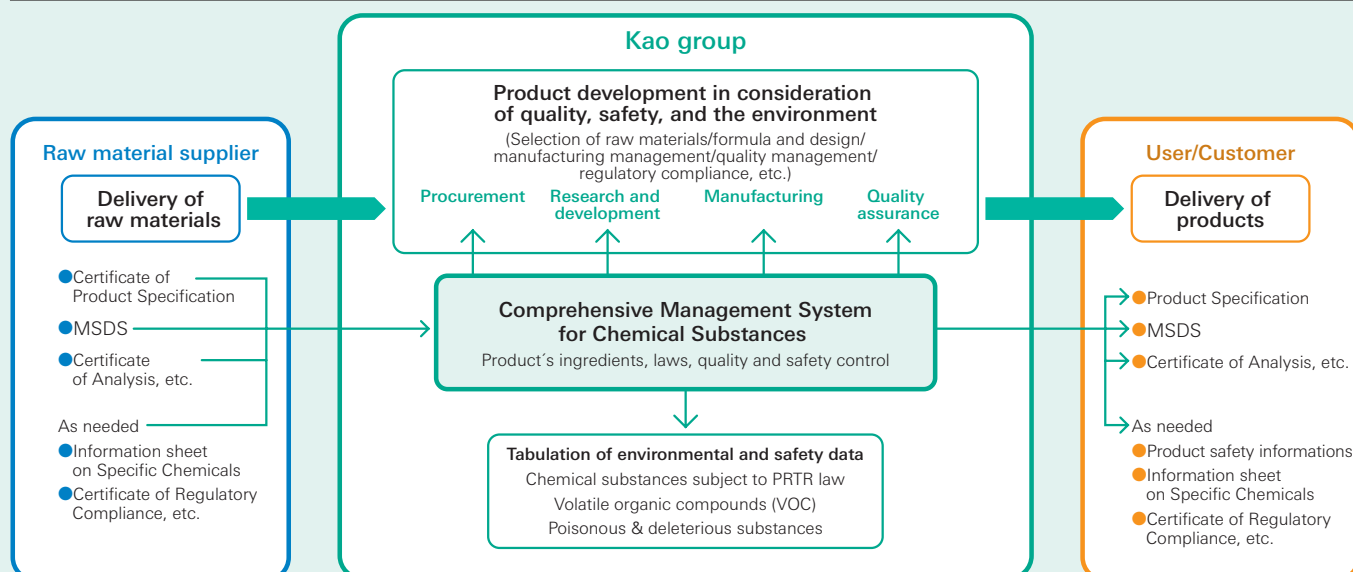
Development of Our Comprehensive Management System for Chemical Substances

The Master Index (MI) is characterized by its hierarchical structure, and consists of consumer products (M1), chemical products (M2), raw materials (M3), and ingredients (M4). (See page 55.) Consumer products generally use several dozen raw materials, most of which are composed of several ingredients. Previously, in order to identify the ingredients in a product, it was necessary to identify the manufacturer of each raw material used and confirm with the manufacturer the composition of a particular material. However, by using Comprehensive Management System for Chemical Substances with the MI as key codes, it has become possible to determine ingredient composition of a product almost instantly. This makes it much easier to check legal situations and safety information and to calculate related costs. It has now become an indispensable tool for Kao. When we started to operate the system in 2001, our data was still incomplete. However, through the concerted effort by this division, and R&D, Procurement, and Production divisions in verifying each component of the system, we have established an accurate database over the past few years.



Yasuyuki Hattori
Senior Manager
Technical Regulatory
Affairs Center

Overview of Kao's Comprehensive Management for Chemical Substances



Checking product quality and safety at each phase of product development based on Kao's standards

Kao promotes total quality management activities from the consumers' point of view considering every stage from their choice and use of products to their disposal, so that consumers can use Kao products with a sense of security.

Consumer driven quality assurance activities

Kao's products are used in various situations in consumers' daily lives. At product development, we check the functions, performance, and user-friendly products from the results of repeated field trials and from the opinions of product testers. We further check the quality of raw materials, containers, packaging materials, and finished products, assuming various situations from purchase, usage to disposal.

The ground for Kao's quality assurance activities is our consumer driven policy "Consumers to Decide on the Quality of the Products." (See the basic policy on quality assurance on page 54.)

Safety assessment serving as the basis of quality

To confirm appropriate safety for human health, effects on the environment, and safety of food products, Kao conducts various safety assessment tests on raw materials and products and implements scientific risk assessments. To facilitate such safety assessments, Kao has drawn up the Kao Safety Assessment Standards for Products and Materials to enact our own strict standards and assessment procedures suitable for product characteristics.

Appropriate assessment procedures and methods are prepared for each product category, and the Safety & Microbial Control Research Center, an independent internal organization

separate from product development, carries out safety assessment for all the raw materials we use and the products we make. After broad-based examinations at the Product Safety Study Meeting comprised Product Quality Management Division, Safety & Microbial Research Center, Consumer Communications Center, Products & Lifestyle Research Center, Research Center for Characterization and Analytical Science, etc., only those products that are confirmed to be safe are launched.

HP Quality Management Activities

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

Promoting development of alternatives to animal testing

As for animal protection, Kao is engaged in developing alternatives to animal testing for skin irritation and sensitization, as well as eye irritation. In tandem with its own efforts, Kao works with the government and other companies in its development activities, and makes public study results by presenting them to academic societies and in academic journals.

Conducting thorough safety and quality control after product launch

Based on specified control standards, Kao implements thorough safety and quality controls on its products and ingredients—even after market launch. We collect information on safety and quality widely from consumer inquiries, literary documents and scholarly information, information from administrative organs and industry organizations, reports by mass media. We always examine such information to see if there are any problems or points that need to be addressed. To prepare for possible serious events, Kao has established a framework to take the necessary measures promptly, such as making announcements and recalling products, placing ultimate priority on safety. All divisions of Kao strive to enhance quality by improving products, reviewing quality control, and making labeling and information easier to understand, so that consumers can use Kao products with a sense of security and feel joy and satisfaction with our products.

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.

Column

Total Quality Improvement Activities

Our efforts for quality represent the implementation of *Yoki-Monozukuri* itself. We perceive "quality" from a total viewpoint. Not only we make sure products are safe, free from defects, and comply with laws, but also we try to offer attractive product with high quality such as highly effective, easy to use, easy to understand, and giving pleasure in use, as well as to ensure management quality, including corporate social responsibilities. Our quality assurance activities also include consistent efforts for quality improvement. At Kao, meetings on product quality are held everyday throughout the company. We value discussions from various points of views by Consumer Products Business, R&D, Production & Engineering, Consumer Communications Center, and Product Quality Management Division. I believe that through each employee's enthusiasm, dedication, spirit of challenge, and steady efforts, that we can fulfill our responsibilities to society and customers as well as offer products that bring out consumers' gratitude. We will continuously live up to consumers' expectations regardless of the many difficult challenges we may face.



Hideko Aoki
Vice President,
Product Quality
Management Center

Quality assurance and traceability of food products materials

For every raw material that is to be used in our food products, Kao confirms legal compliance and information on traceability, such as original materials*¹ and place of origin by tracing them back to their origins and cultivation and has concluded contracts with material suppliers using Certificate of Product Specification. We monitor our quality assurance arrangements by confirming contract contents and management systems through conducting periodic audits and quality assurance meetings. We have established traceability that can trace original materials used for raw materials from a product lot number.

Control standards for agricultural chemical residues, etc.

Related laws on a positive list system*² for agricultural chemical residues were promulgated and became effective in May 2006. In advance of the enforcement, in May 2005 Kao started to operate agricultural chemical residues control standards, keeping pace with the positive list system.

Kao's agricultural chemical residues control standards are as follows:

- 1) Obtain information on the use of agricultural chemicals, analytical data from material suppliers for every food product material. Confirm that there are no problems

concerning agricultural chemical residues.

- 2) For key materials (such as oils to be used in *Econa* cooking oil, tea leaves and catechin to be used in *Healthy* tea drink), investigate the actual conditions at the places of origin to confirm that there are no problems.
- 3) For all products and key materials, periodically analyze agricultural chemical residues to confirm that there are no problems.

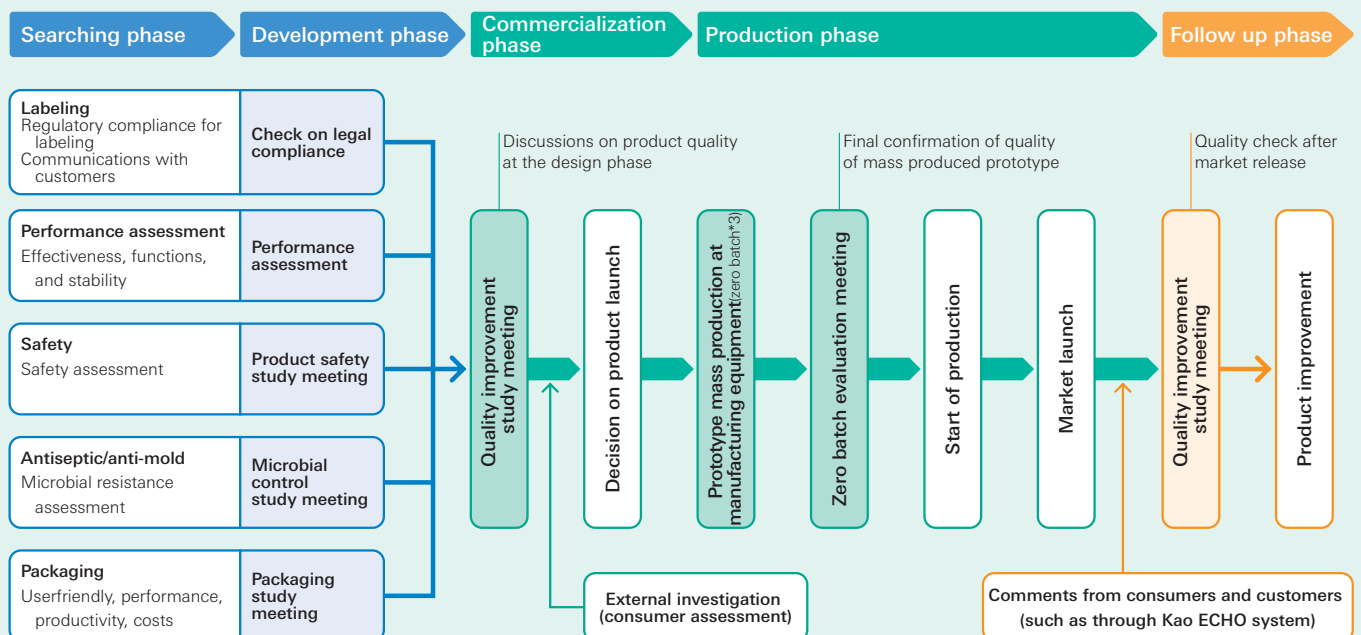
News report on the safety of products

In August 2005, some media reported on the safety of Diacylglycerol, one of the main ingredients of *Econa* products and Kao received a number of inquiries from consumers. Having conducted safety evaluations from various viewpoints, Kao has judged that there are no problems in safety. Please refer to our Web site for details.

HP Media report on the safety of *Econa* Cooking Oil
<http://www.kao.co.jp/econa/050920> (only available in Japanese)

- *¹ Original materials: Refer to primary agriculture, livestock, and fishery products themselves. For example, an original material of soy sauce is soy.
 *² Positive List System: A system that prohibits, in principle, the distribution of foods that contain agricultural chemicals unless maximum residue limit for them are established under the Food Sanitation Law.

Quality Management Flow



*³ Zero batch: Experimental manufacturing of a product as a final confirmation under actual conditions using the actual manufacturing equipment and final containers.

Conducting integrated management for the environmental conservation and occupational safety

Kao promotes integrated management in line with Responsible Care (RC) activities, an initiative by the chemical industry for self-management, to conduct business and develop products, while paying due attention to the safety of employees, local residents, and the global environment.

RC management

Kao implements its environmental and safety management system in line with the basic five elements of Responsible Care (RC), the chemical industry's initiative for self-management activities and based on the element "to conduct dialogue with society." (See Basic philosophy and policies on the environment and safety on [page 54](#).) Kao reinforces its internal auditing every year and confirms that the PDCA cycle is implemented properly.

At the same time, environmental and safety performance is shared company-wide and a database has been independently developed and operated in order to enhance data reliability and transparency. The database, called "Kanchan" stores environmental impact data and occupational injuries and accidents reports. The system can automatically calculate greenhouse gas emissions and occupational accident frequency rates.

In the future, environmental data at all domestic and Asian factories will be shared. Staff at each factory will be able to check other factories' environmental impact status via our intranet. This should reinforce Kao's efforts to improve environmental and safety programs even further.

Data shared:

Energy use, greenhouse gas emissions, SOx and soot and dust emissions, soil and ground water measurements, PRTR material

Column

Efforts for the Environment and Safety

Kao is a company that deals with chemical substances and it is one of its corporate-wide priorities to assure the safety of employees and all customers, and to protect the global environment throughout the entire product lifecycle from development, production, distribution, and consumption to disposal. It is also our hope that we contribute to the realization of a sustainable society and to comfortable lifestyles of people all over the world through these initiatives. In addition, in accordance with the Philosophy of Responsible Care, a global initiative by the chemical industry, Kao has thoroughly promoted the RC concept, enhanced management structures, established a database and, implemented a variety of related measures. At the same time, we need to recognize that our lives enjoy nature's various changing moods, resulting from the soundness of the ecosystem. In response to global environmental problems, such as the vanishing biodiversity, Kao will reinforce its activities in environmental conservation, the restoration of lost nature, and sustainable utilization, as a part of our efforts to create a society that coexists with nature. In recent years, environmental problems have become a global issue that entails not only local approaches but also integrated, global approaches. We will continue our efforts to create a society in harmony with nature from an overall optimum viewpoint, while keeping close contact with our work-fronts.



Tadashi Matsui
Vice President,
Environmental and Safety

amounts and emissions, waste materials generated, discharged and finally disposed, occupational accident statistics, traffic accident statistics, etc.

Continuous environmental and safety education

Kao continuously educates its own employees and the staff of its business partners based on the ISO management system and occupational safety and health management system in its RC activities. Education and awareness promotion for RC activities are promoted by the Responsible Care Promotion Office and divisional supervisors. In the Production & Engineering Division, where environment and safety education is indispensable, various sessions are held for different levels of personnel. Quite a number of engineers and operators from overseas manufacturing centers participate in the sessions. (For details of the educational sessions held, [See page 54](#).)

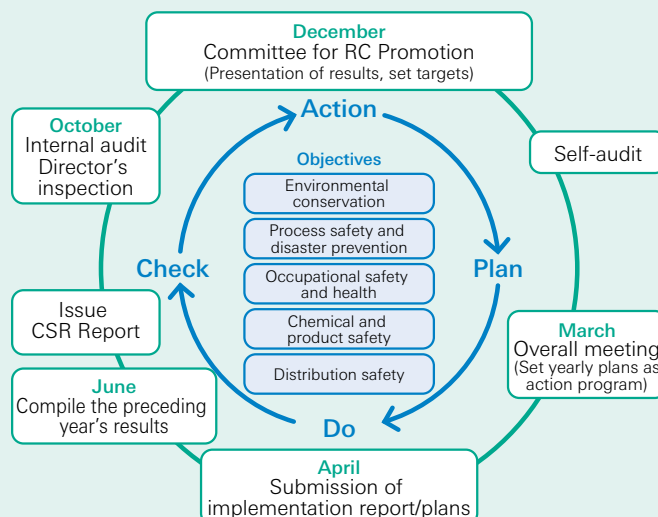
Safety of employees and local residents

Kao believes that the safety of employees and local residents are naturally of prime importance. Kao is engaged in daily production activities, based on the belief that we cannot achieve *Yoki-Monozukuri* without harmonious coexistence with local residents.

The health and safety committee improves working environments and facilities and provides safety education and training for employees in order to eliminate occupational accidents. At factories, based on the Occupational Safety and Health Management System (OSHMS), risk assessment is continuously underway.

In preparation for serious disasters or accidents, Kao has established process safety and disaster prevention rules. For detailed disaster prevention activities and responses to disasters, we have formulated disaster prevention guidelines and a relief aid supply outline.

Annual Schedule for RC Activities



These guidelines and outline have provisions on support activities and relief aid supply to local communities. In time of disaster, Kao will promptly provide support for local communities according to the nature of the situation.

Safety of the global environment

Kao has established and is implementing standards and mechanisms that pay attention to the environment from various viewpoints at each stage of material procurement, product development, production, use, and disposal. Each factory has established specific numerical objectives for energy saving, reduction of greenhouse gas emissions, waste materials, and chemical substance emissions. We are engaged in activities aiming to achieve the objectives and regularly measure our environmental performance. We also endeavor to dispatch information through our Web site to enable consumers to use our products as a part of their environmental considerations.

Kao operates the following standards, rules and mechanisms: Green Purchase and Procurement standards, Comprehensive Management Standards for Chemical Substances, Standards for Environmentally-Conscious Design and Operative Provisions, 5 Principles of Product Development, Product Safety Study Meeting, and “Kanchan” (the Environmental & Safety Data Management System).

Consideration for both natural and artificial cycles

Domestic wastewater that includes consumer products such as laundry detergent is treated by artificially-controlled sewage treatment facilities or decomposed by microorganisms inhabiting the rivers before returning to the natural cycle, such as in rivers, lakes, and oceans. Because the plastics used for containers and packaging are not

biodegradable, they are recycled by an artificial circulation system or incinerated to be returned to nature's cycle.

As explained above, the treatment of used products at household depends on two purification and circulation systems—natural and artificial. Kao's basic policy of environmentally-conscious design is to reduce environmental impact throughout a product's lifecycle without creating excessive burdens on these two purification and circulation systems.

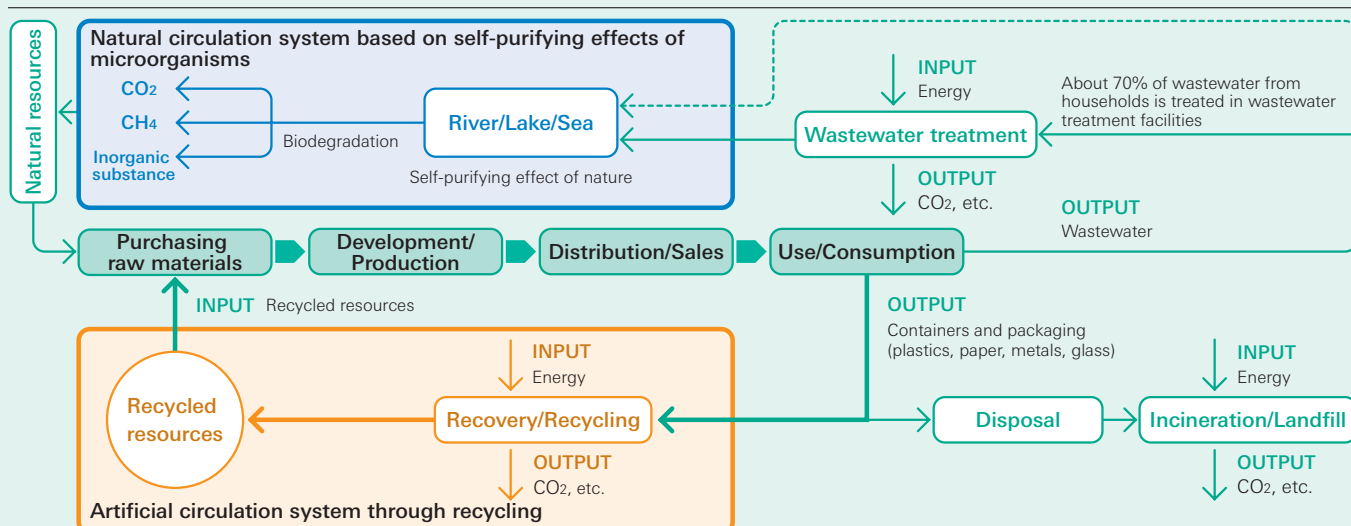
Assessing the environmental safety of surfactants

In accordance with our environmentally-conscious design standards, Kao strives to develop products having high biodegradability (used substances are degraded by microorganisms in the natural environment) and that place less impact on various ecosystems, such as those of aquatic organisms. Kao also pays close attention to the negative impact of products when they are disposed of into rivers and the natural environment. To this end, we are participating in an environmental monitoring investigation by the Environment, Health and Safety Task Force of the Japan Soap and Detergent Association, in cooperation with other member companies. We measured the concentration of four types of surfactants subject to the PRTR Law, such as LAS at the Tama River, and three other rivers flowing in urban areas, four times a year. As a result of the assessment of risks to the ecosystem based on the fiscal 2004 tests, it was confirmed that the concentrations of these surfactants were lower than the level allowable to ecosystems and that the risk of these surfactants to ecosystems is very low, as it had been up to fiscal 2003.

HP Japan Soap and Detergent Association

<http://jsda.org/> (only available in Japanese)

Natural and Artificial Circulation System





Highlights of CSR Activities in FY 2005

Kao is promoting its CSR activities in consideration of balancing the triple bottom lines of economic, social, and environmental activities. The following is a summary of our main topics in fiscal year 2005.

1 Acquisition of stocks of Molton Brown of the U.K. and Kanebo Cosmetics

In July 2005, Kao purchased the stocks of Molton Brown in the U.K. This company manufactures and sells skin care, hair care, and body care products. We intend to establish a close cooperation with Kao subsidiaries in Europe and the United States to expand our operations more globally. In January 2006, we acquired the Kanebo Cosmetics stocks, and we intend that this company will play a principal role in Kao's beauty care business. (See page 52.)

2 Participation in the Global Compact

In May 2005, Kao signed the United Nations Global Compact to further promote our CSR activities in and outside Japan. (See page 53.) The Global Compact holds up the 10 principles in relation to human rights, labor standards, the environment, and anti-corruption. The Kao group is currently monitoring its compliance with the ten principles. (See page 33.)

3 Meeting on consumer consultation in Asia

In November 2005, a meeting for managers in charge of consumer consultation in the Asian region was held. Consumer consultation staff gathered from the region to share information about each country's consumer consultation situation, to discuss better consultation practices, and to identify problems. (See page 28.)

4 EMAS certification of Kao Corporation S.A.

Kao Corporation S.A. was certified under the Eco-Management and Audit System (EMAS), an environmental management system implemented voluntarily by companies operating in the EU. EMAS-certified companies are required to undergo a check on their environmental performance by authorized organizations every year and to make these audit results public. In response, Kao S.A. issued its first environmental report in English and Spanish. (See page 50.)

5 Establishment of Internal Control Committee

In September 2005, the Internal Control Committee, chaired by the President, was established. Functions related to internal control, such as disclosure, compliance, risk management, and internal auditing, were previously performed by individual committees and divisions. These functions have now been integrated across the company to this new committee in order to improve the quality of business operations. The Committee is responsible for all internal control activities in general as an executive entity within the Management Committee. (See page 20.)

6 Establishment of Kao Peony to provide job opportunities to the intellectually challenged

In October 2005, Kao established a wholly-owned subsidiary called Kao Peony. The company was approved as a special subsidiary in April 2006 and started its operations. With a view to providing a dedicated workplace for people with intellectual disabilities, the subsidiary packages products and samples. (See page 32.)



7 Cosponsorship of the third Japan Science & Engineering Challenge (JSEC)

Kao joined as a cosponsor of JSEC as a part of Kao's efforts to nurture the next generation, as a theme for its social contribution activities. JSEC is a contest for independent research in science and technology for high school students. The Kao Prize was awarded to a research project entitled, "Research on the proliferation of lady-slipper, an endangered species—development of a culture base and aerobic culture method based on growing environment study." (See page 40.)

8 Reception of the Grand Prize in the fourth Key Firm of Integrity Award

In March 2006, Kao was awarded the Grand Prize in the fourth Key Firm of Integrity Award. This prize is given to a company that practices progressive approaches in communication structure and check mechanisms in terms of compliance, after due investigation and inquiry to the nominees.

HP Announcement of the fourth Key Firm of Integrity Award

<http://www.kfikk.co.jp/newsdata/AWARD2006.pdf> (only available in Japanese)

9 Participation in the "Team Minus 6%" campaign

Kao participated in a national campaign called "Team Minus 6%" promoted by the Ministry of the Environment to prevent global warming. Kao set air conditioning at 28°C at offices and staff were allowed to wear light casual clothing ("Cool Biz") in the summer. At storefronts, signs on Cool Biz and Warm Biz were displayed with our laundry finishing products to raise consumers' awareness. (See page 45.)



Main CSR Topics in FY 2005

The following provides details of the progress made in Kao's CSR activities.

Item	Achievements in FY2005	Page in this report
CSR promotion	Participated in the U.N. Global Compact	P. 18
Quality assurance	Reorganized responsibility structure in response to the revision of the pharmaceutical law	P. 19
Responsible Care	Reinforced the organization of the Committee for Responsible Care Promotion	P. 19
Corporate governance	Established the Internal Control Committee	P. 20
	Considered the development of a business continuity plan	P. 21
Compliance	Prepared the global standard edition of Kao's Business Conduct Guidelines	P. 22
	Reinforced compliance education at overseas group companies	P. 22
Communication with consumers	Inauguration of Products and Lifestyle Research Center, which studies consumer perspective and awareness	P. 28
	Held Asia Consumer Communications Manager Meeting to enhance consumer consultation service outside Japan	P. 28
Relationship with customers	Implemented RC patrol at distributors of chemical products	P. 30
Relationship with suppliers	Adoption of the Guidelines for Procurement of Raw Materials	P. 31
	Started preparing the standards and undertaking preliminary studies for CSR based procurement	P. 31
Relationship with shareholders and investors	Corporate dividend increased for the 16th consecutive year	P. 21
Relationship with employees	Established Kao Peony Co., Ltd., a special subsidiary that provides job opportunities to the intellectually challenged	P. 32
	Improved systems to support work-life balance	P. 32
	Conducted the 3rd Employee Opinion Survey	P. 33
	Conducted compliance survey of Kao group companies outside Japan regarding human rights and labor standards	P. 33
	Implemented internal survey/measures to address asbestos issues	P. 35
Relationship with society	Conducted an external evaluation of social contribution activities	P. 36
	Held the 3rd debriefing session by recipient organizations at employee donation organization	P. 37
Environmental reporting	Took part in the "Team Minus 6%" campaign	P. 45
	Final waste disposal amount reduced to one-fourth	P. 47
	Established a system to share information on contract waste disposers	P. 47
	Five domestic factories issued site environmental reports	P. 50
	Kao Corporation S.A. issued an environmental report	P. 50
Communications	Issued the first CSR Report	P. 59
	Held Stakeholder Dialogue with employees	P. 59

Management Systems

Supporting CSR activities with a company-wide structure

Propelled by the Global Compact, Kao identifies challenges in its CSR activities through company-wide committees and prompts action by the relevant divisions.

System for CSR Promotion

Previously, each division was engaged in its own CSR activities. In July 2004, Kao established the CSR Committee and CSR Department to integrate such divisional efforts into overall group activities. The CSR Committee, chaired by the President and CEO, comprises representatives of divisions concerned with all aspects of CSR. At bimonthly meetings of the Committee, under the leadership of the chairman, CSR challenges that face the entire company are discussed so that the divisions can then tackle such challenges. Each division has been reinforcing its CSR efforts each year and is currently addressing such CSR challenges as dialogues with stakeholders, activities to conserve the global environment, the introduction of CSR activities into the supply chain, and respect for the diversity of our employees.

Meanwhile, we still have a major challenge of implementing our CSR activities on a global scale. To this end, in May 2005 Kao signed the United Nation’s Global Compact, one of the representative international CSR initiatives. By appealing our stance for respecting the Global Compact’s ten principles and our efforts to this end both inside and outside Japan, and by joining in global networks, we will enhance our CSR activities as a concerted initiative of the Kao Group.

Group-wide efforts to raise CSR awareness

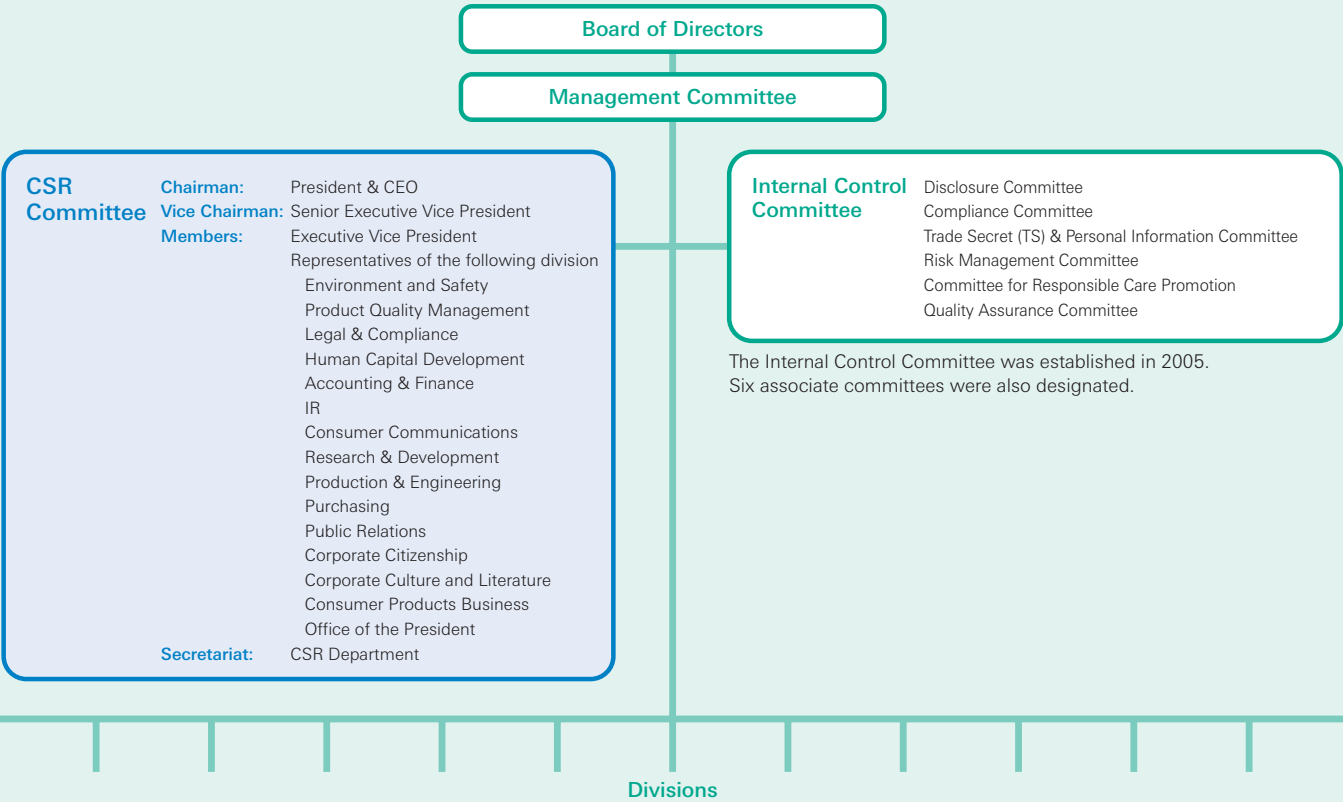
We believe that participation-based activities are indispensable for CSR. Kao endeavors to educate employees to make sure that all employees understand the status quo and tackle challenges accordingly. In fiscal year 2005, to deepen employees’ understanding of Kao’s CSR activities, CSR Reports were

distributed to about 15,000 employees of domestic group companies and 1,600 copies of the English version of the report were distributed to overseas group companies.

Also, in the employee opinion survey, “Find,” conducted last year, (See page 33.) we asked employees what were their opinions of CSR. Of approximately 12,000 domestic group company employees who responded, 10% of respondents still answered that they didn’t know the term CSR or they were not interested in CSR. The CSR Department views this result as one of the important issues to be resolved through CSR promotion. We analyzed the survey results by group company and by division, drew up appropriate action plans to promote employees’ awareness of CSR and their understanding of CSR concepts. We will also reinforce our efforts to promote CSR awareness in our overseas group companies.

CSR Structure

(As of March 31, 2006)



Product quality management system

As for activities concerning product quality management in the Kao group, the Quality Assurance Committee, a subordinate committee of the Internal Control Committee, has been established to deliberate and decide on basic quality policies and important measures, as well as to monitor the effectiveness and reliability of quality management activities. The Product Quality Management division formulates basic quality policies and important measures and proposes them to the Quality Assurance Committee. The division undertakes a role of supervising and promoting quality management activities. In line with the revision of the pharmaceutical law that came into force in April 2005, the head of Product Quality Management serves as "Marketing Supervisor General" who is in charge of safety and quality control. "Post-marketing Safety Manager" and "Quality Assurance Manager" are also assumed by managers of Product Quality Management.

Furthermore, for each business segment,

a Quality Assurance Meeting and a Quality Improvement Study Meeting have been established, participated in by managers of Global Consumer Products, Research and Development, Production & Engineering, Consumer Communications Center and Product Quality Management, etc. Kao is engaged in company-wide quality management activities based on the consumer driven approach that "Consumers to Decide on the Quality of the Products."

Responsible Care (RC) Promotion System

RC activities are promoted on the initiative of each division and supported by the Responsible Care Promotion Office and divisional members of the Committee for Responsible Care Promotion. In September 2005, the Committee for Responsible Care Promotion became an associate organization of the Internal Control Committee and is attended by members of responsible care promotion from each division. Members participate in corporate planning, deliberations, and decision-making

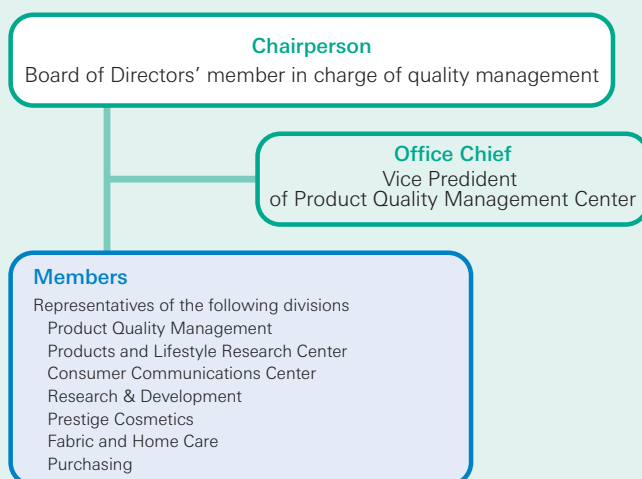
concerning each division's targets and plans, and undertake the role of actively promoting RC activities. This has enhanced our RC activities towards more thorough-going and responsible activities. RC activities at office buildings are also enhanced by clarifying such activities in the General Affairs department.

Results of internal audit on RC activities

Although the audit results showed no significant nonconformities, some issues were found to require continued monitoring (See page 54.) because of inadequate revisions of divisional guidelines and an organization chart. The production sector, recognized for its progress in its activities, will enhance its activities towards further improvement. The research & development and business sectors, found to be insufficient in the practice of environmentally-conscious product design, will make greater efforts. Although some improvements were observed for affiliate companies, they are still insufficient. Broad-based implementation across the company is therefore necessary.

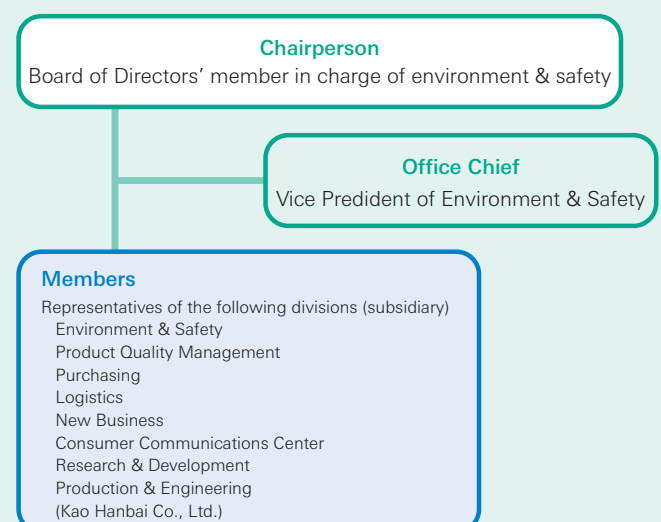
Quality Assurance Committee

(As of March 31, 2006)



Committee for Responsible Care Promotion

(As of March 31, 2006)



Continuing corporate governance reforms

Kao has been consistently reforming its corporate governance to continue growth and fulfill its corporate social responsibilities. We separate the functions of supervision and execution of management and, in order to ensure appropriate governance, implement auditing through various supervisory systems.

Promoting continuous corporate governance reform

Basic concept and management structure

Kao's basic position on corporate governance is to develop a managerial framework and internal control system that can take the necessary measures to realize highly efficient, sound and transparent management with the aim of continuously increasing corporate value. Kao considers corporate governance to be one of its most important managerial tasks.

Kao introduced an outside director and executive officer system in 2002 as a system to promote the separation of supervision and execution within the conventional framework of directors and auditors.

Chairman/President appointment process, and evaluation and compensation of directors and executive officers

Kao has established the Committee for the Examination of the Nominees for the Chairman of the Board of Directors and

the President and the Compensation Advisory Committee to serve as bodies to perform similar functions to a nominating committee and a compensation committee, respectively, in a company with three committees under the Corporation Law. The former consists exclusively of outside directors and outside corporate auditors. The latter consists of a representative director, the Chairman of the Board of Directors and all the outside directors. Regarding remuneration for members of the Board of Directors and executive officers, Kao has implemented a stock option plan for the purpose of aligning their interests with those of shareholders of the company. Kao applies performance-linked remuneration, based on EVA (Economic Value Added,) etc.

Various internal and external supervisory structures

Corporate Audit Services were established to audit the appropriateness of operational process and management adequacy and efficiency of the Kao Corporation, including domestic and overseas affiliate companies. Currently,

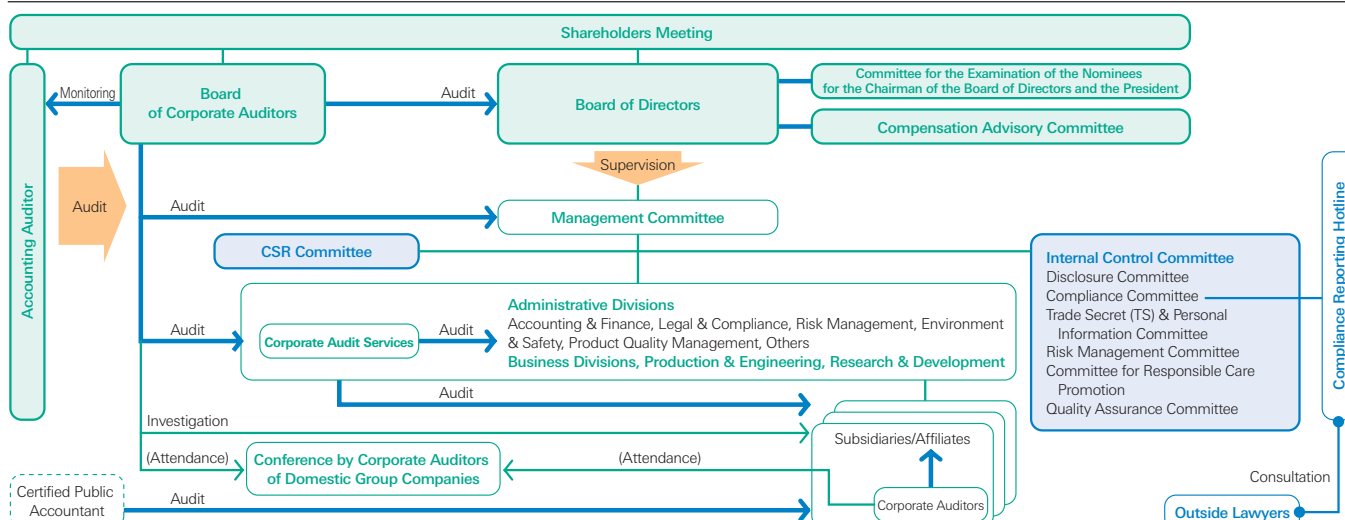
four corporate auditors, including two outside corporate auditors, exchange opinions regularly with representative directors, attend meetings of the Management Committee and other important meetings, participate in regular Conferences by Corporate Auditors of Domestic Group Companies, and exchange auditing information with the internal auditing division and accounting auditor, as necessary. Kao strives to improve the effectiveness and efficiency of its auditing practice through these arrangements.

The Internal Control Committee, chaired by the President and CEO, was established in September 2005. It discusses and makes decisions on basic policies and operating plans related to internal controls, as an operating entity of the Management Committee. As related organizations of the Internal Control Committee, six associated committees were established to promote group-wide internal control initiatives throughout the Kao Group companies.

HP Kao's corporate governance

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

Corporate Governance Structure



As of the end of March 2006, in its management structure, the company has 15 members of the Board of Directors, including two Outside Directors and the Chairman of the Board of Directors without representative rights, and 19 Executive Officers, including 11 who serve concurrently as members of the Board of Directors.

Committee for the Examination of the Nominees for the Chairman of the Board of Directors and the President: At the election or re-election of the Chairman/President, this Committee examines the suitability of candidates in advance and advises the Board of Directors.

Compensation Advisory Committee: This Committee judge the appropriateness of the compensation programs and levels applied to the members of the Board and to executive officers.

Ensuring company-wide risk management

Risk Management Policy and organizations

Of risks that could occur during own business activities, risks associated with management strategies are analyzed and their countermeasures are discussed by relevant divisions in advance. When necessary, such risks are discussed by the Management Committee and the Board of Directors.

As to risks in business operations, group-wide risk management activities are conducted based on the Risk Management Policy, in particular by the Risk Management Department established in 1999.

Basic activities place emphasis on two points: 1) risk prevention and control; and 2) crisis management in the case where a risk materializes and a contingency occurs.

Identifying risks by division and responding through company-wide efforts

Risks such as disasters, accidents, and

quality problems are classified and we assign each classified risk to relevant divisions. While each division studies divisional risks, the Risk Management Department endeavors to identify cross-divisional risks and the risks for which no specific division is responsible and to draw up countermeasures. The Office holds a risk management promotion liaison meeting with divisional staff in charge of risk management promotion. The liaison conference examines the implementation of risk management activities by each division and creates standards to identify and manage risks.

To deal with risks involving overseas operations, which earn one-fourth of Kao's consolidated sales, overseas risk management meetings are held bimonthly to exchange information. A framework for overseas risk management has been established, such as resident officer training programs and communication hotlines.

Prevention, initial actions and BCP

Kao aims for the prevention of accidents and disasters, as well as product and overseas business-related risks and has

proposed initial actions and a Business Continuity Plan (BCP) as priority themes for fiscal year 2005.

BCP consists of business impact analysis on business operations and formulating, implementing, and operating a Business Continuity Plan. This is in an effort to continue critical business operations in the event of a major disaster. To this end, Kao has examined its operations from various aspects, such as setting a priority on business tasks, possibility of alternate production at other factories, developing lines of command, and securing important business bases.

Column

Communication with Shareholders and Investors

Kao has actively endeavored to ensure highly transparent information disclosure to shareholders and investors and holds dialogues with all interested parties. Through the participation by senior management in dialogues with investors, Kao has successfully earned the market's trust. We won Best Disclosure Award from the Tokyo Stock Exchange for our performance, particularly for the way in which the President personally provides answers to questions on growth strategies, which attracts great attention from investors. Our activities of incorporating investor and market feedback into management through IR activities were also recognized.

Kao sends convocation notice to shareholders more than four weeks before Annual General Meeting of Shareholders so that our shareholders can have enough time to examine the agenda. For the convenience of foreign shareholders, we also prepare an English translation of the convocation notice and post it on our Web site. Explanations and resolutions at the meetings are also disclosed on the Web site, both in Japanese and English.

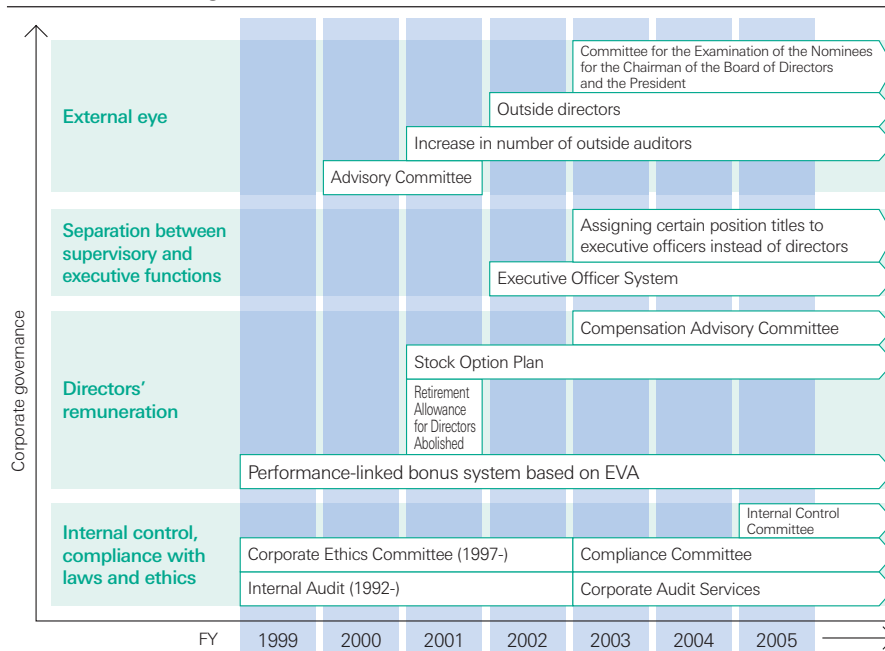
Dividend increased again in 2005, recording increased dividend for the 16th consecutive year. (See page 52.)

HP Web page for investors
<http://www.kao.co.jp/en/ir/>



Annual General Meeting of Shareholders

Continuous Management Reform



More reliable corporate activities through stricter compliance

Kao performs corporate activities to earn a respect of society as an honest, sincere, and virtuous company through its sensible and fair business practices, guided by ethical conduct and compliance with laws.

Reinforce a compliance structure

Basic compliance policy and Compliance Committee activities

Consumers have become increasingly severe judges of companies year by year in the wake of recent corporate scandals. Kao holds up “Integrity” as one of its basic values in The Kao Way and advocates that the company will live up to the support and expectation of all stakeholders by acting based on legal and ethical principles that go beyond more compliance with laws and conducting honest and clean business activities.

We also adopted the Kao’s Business Conduct Guidelines (Kao BCG) (See page 53.) as action guidelines for employees in their daily work. We strive to always be an open and transparent company through making internal and external hotline reporting services available to employees and conducting compliance training programs on a regular basis. Through these efforts, Kao ensures that its concept, “compliance is an activity of employees, by employees, and for employees,” is in place throughout the company so that each of the employees can work spontaneously and confidently.

Status of the Compliance Committee changed

Kao established the Compliance Committee, chaired by the Executive Vice President, comprising representatives of

relevant divisions and affiliate companies. With the establishment of the Internal Control Committee in September 2005, the Compliance Committee became one of the associate committees of the Internal Control Committee. This facilitated cooperation between the members of Disclosure Committee, TS (Trade Secret) & Personal Information Committee and other associated committees. (See page 20.)

The Compliance Committee revises the Kao BCG, organizes programs to promote the introduction and establishment of corporate ethics, provides reliable hotline reporting services, and reviews and monitors the status of concerns. These actions are reported and proposed to the Board of Directors.

Wider implementation of the Kao BCG

In fiscal year 2005, Kao formulated a global standard version of the Kao BCG and promoted its introduction in overseas group companies. We conducted compliance training programs for the newly appointed presidents of overseas group companies, clarify the person who is in charge of compliance issues at each company, and engaged in the development of TS rules.

Hotline reporting services

To respond to whistle blowing on illegal or unethical conduct, Kao provides hotline reporting services for Kao Group

employees operated by the Compliance Committee secretarial staff and by external specialists, including lawyers. These services are available to Kao Group employees in Japan and some of the services are also available to our stakeholders to solicit their opinions. To reassure employees and attract them into reporting, careful attention is paid to keeping information about informers confidential, and unfavorable treatment to informers is prohibited for the reason that such reporting is made.

In fiscal year 2005, an average of 10 reporting were received every month but none of them represented a serious problem. Reporting from associate companies and contract employees are on the rise. Common problems are fed back into the company on a case-by-case basis, while careful attention is paid to the protection of the privacy of an informer.

Compliance audits and monitoring

The following are some of the activities conducted regularly: internal audits on compliance by the Corporate Audit Services, conducted a survey called “Find,” for all employees, (See page 33.) self-diagnosis for the divisions to which they belong by Compliance Committee members, and self-check exercises for compliance practice for training seminar participants. Kao analyzed the results of the survey “Find” in the Kao BCG. The analysis revealed that some of the Kao

List of training programs

- Orientation for new graduates
- Training for mid-career entrants
- Training to support indispensable tasks at job family revision
- People management training
- Training to support indispensable tasks at rank revision
- Legal training for business leaders
- Basic training for overseas senior management



In-house seminar

employees are still not in mind of compliance. It showed that the levels of awareness of compliance significantly vary depending on departments, while the administrative divisions show high levels of awareness. We will implement measures to enhance the awareness of less conscious employees and divisions.

Compliance training results and participants' voices

We conduct compliance training programs at various opportunities, including management seminars organized by the Human Capital Development Division. In fiscal year 2005, training programs were provided to more than 500 employees. To promote all employees' awareness and study of compliance, case studies of other companies are periodically published, and inquiries and answers thereto made to/from the Compliance Department are published via an intranet.

Strengthening the function of Legal Experts

It is very important for every Kao division to understand legislation related to their businesses. Persons in charge of relevant legislation are designated at the respective divisions and registered as legal experts. As of the end of March 2006, there were a total of 341 Legal Experts registered for 246 legislations. This represents an increase by 14 legislations and 19 Legal Experts from

the previous year reflecting the laws covered by the Whistleblower Protection Act, etc.

Legal Experts are responsible not only for division-specific issues, but also for company-wide issues. In fiscal year 2005, some Legal Experts held study meetings for staff across the company. In order to clarify the company's regulation to be complied with by employees at anytime, the Company Regulation System has been established on the intranet to facilitate the observance of company regulations.

Information security and protection of personal information

Kao has established Guidelines on Handling Trade Secret Information, Guidelines on Handling Personal Information, and IT Security Guidelines, based on its Information Security Policy. We enforce our information security management within the framework of the Trade Secret (TS) & Personal Information Committee, divisional members for protection of trade secrets, and supervisors for administering personal information. Kao will also continue to further train these personnel and other employees.

Kao retains a large amount of personal information concerning participants for promotional campaigns, consumer monitors and callers of the

Consumer Communication Center. Kao makes steady efforts pursuant to Personal Information Protection Law and the Ministry of Economy, Trade and Industry's guidelines to protect such personal information. When Kao consigns transactions involving personal information to other companies, we always exercise thorough oversight of them by means of detailed contracts and auditing procedures. We also securely protect the personal information of Kao employees pursuant to the Ministry of Health, Labour and Welfare's guidelines.

Future issues and plans

Kao will continue its compliance activities and enhance the employee's awareness of compliance issues. We will also establish organization for the compliance at both domestic and overseas subsidiaries and affiliated companies.

Column

Have participated in a compliance training program

I learned about Kao's Business Conduct Guidelines (BCG) for the first time in my introduction training. Before I actually studied them, I was afraid that the guidelines might be difficult to understand. However, there were actually many concerns that we could practice immediately. In my impression, the items of the BCG are not something special, but something that can protect us employees. I understand that it is important for us to conduct daily work complying with BCG in order to come under the protection of the BCG. I would like to remember the motivated feeling when I first learned about BCG and enjoy my work as an employee of Kao.



Rie Kawamura
Human Capital Development

Roles of Legal Experts

- Provide counseling and advice to employees concerning the interpretation of legislations
- Monitor legislative amendments
- Revise internal regulations according to legislative amendments, if necessary
- Promote legal compliance
- Conduct audits or request divisions in charge of auditing

Major external corporate recognition and commendation in FY 2005

Major corporate recognitions from external organizations

Review body/publishers	Title of survey	FY2005 ranking results
Nihon Keizai Shimbun	Nikkei PRISM (Private Sector Multi Evaluation System)	18th
Newsweek (Japanese Edition)	Newsweek Global 500	44th (5th in Japan)
Nihon Keizai Shimbun	Employee-friendly Company	16th
Nikkei Business	100 Most-admired Companies in the area of CSR in Japan	30th
Nihon Keizai Shimbun	Nikkei Quality Management Survey	68th
Nihon Keizai Shimbun	9th Nikkei Environmental Management Survey	168th
Nihon Keizai Shimbun	Nikkei Corporate Image Survey	7th in business people; 9th in general public segments
Weekly Toyo Keizai	1st CSR General Ranking Best 100	17th
FORTUNE	Global Most Admired Company	5th in Household & Personal Products

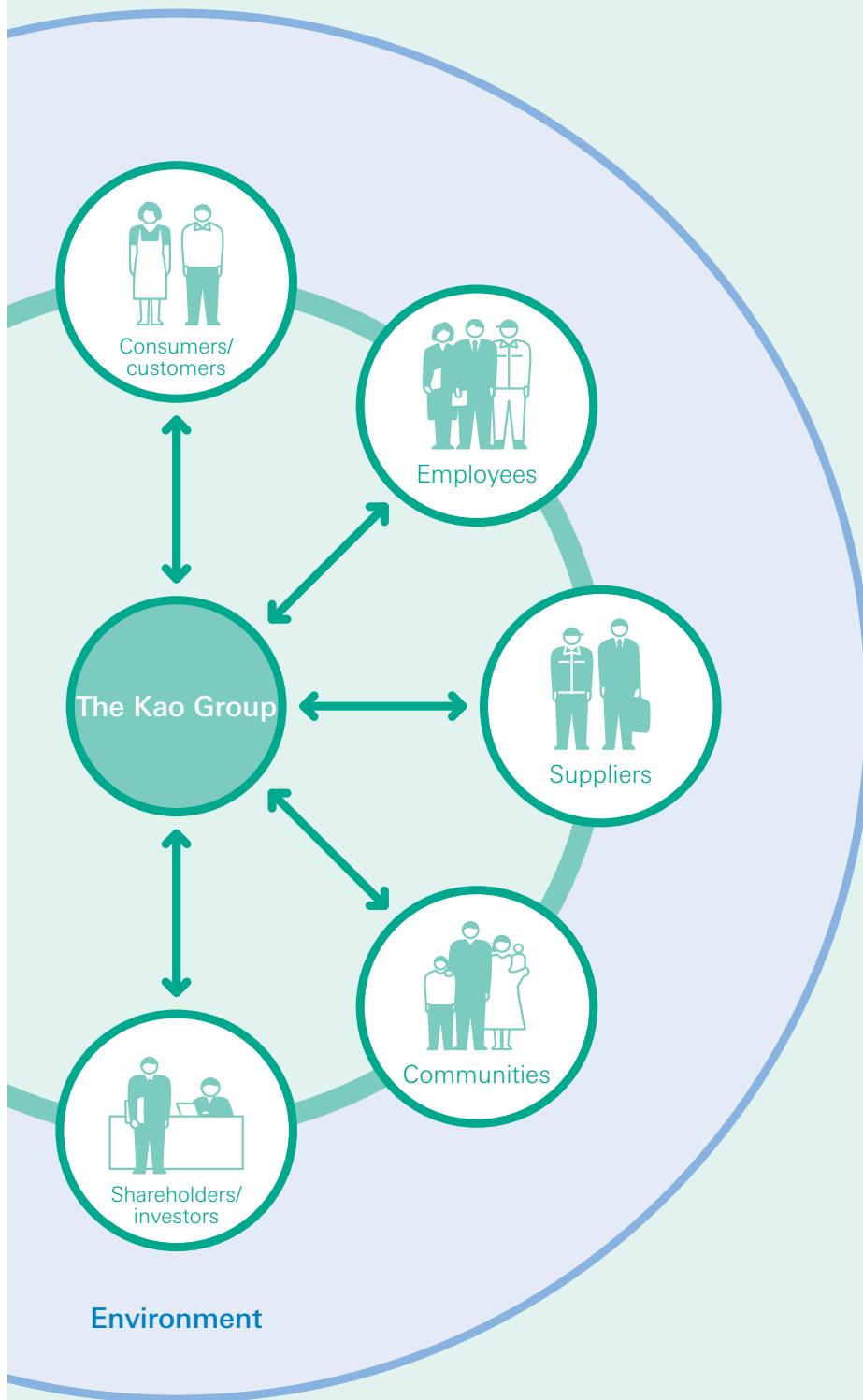
Major commendations from external organizations

Commendation	Description
Minister of Economy, Trade and Industry Award, FY 2005 Intellectual Property merit award	Awarded by the Patent Office in recognition of effective utilization of the Industrial Property Right System through the use of the Crescent Moon logo, a symbol of the company and the launch and development of the <i>Attack</i> and <i>Biore</i> brands, thus contributing to the development of the system.
Asian MAKE Award Winners for four consecutive years	Kao was selected as Asian Most Admired Knowledge Enterprises (MAKE) by Teleos in the U.K. This prize was given to three companies from Japan based on investigations on the level and capability of knowledge management in a company.
4th Key Firm of Integrity Award	Kao received the grand prize of the 4th Key Firm of Integrity Award sponsored by the Sankei Shimbun and Kfi K.K. Kao was highly evaluated and selected for the prize in recognition of the establishment of the Internal Control Committee and its unique Legal Expert system. (See page 15.)
Environmental Technology Award of the 37th Japan Chemical Industry Association Technology Award	Awarded for the development of clean manufacturing method of ether from alcohol and carbonyl compounds using Pd/C catalyst. This environment-friendly manufacturing method enables synthesis of ether from materials with less environmental burden than conventional methods. Byproduct is essentially only water.
FY2005 Society of Chemical Engineers, Japan (SCEJ) Technology Award	Received an award for the development of a manufacturing process of functional composite powders using supercritical carbon dioxide, an environment-friendly product manufacturing technology, in March 2006. It was recognized as a part of efforts to promote "green sustainable chemistry" and received the FY2005 SCEJ Technology Award. (See page 6.)
CEW 2005 Beauty AWARD	Kao Brands Company's <i>Brilliant Brunette Shine Shock</i> won the CEW 2005 Beauty AWARD, known as the "Oscars" of the beauty industry, selected by industry participants. The product's effectiveness was recognized and commended for being the first hair care series for women with brunette hair.
Health care study video received award at the Industrial Film Contest	Kao's health care research video won the Nippon Keidanren Chairman Prize at the Japan industrial film contest held by Japan Industrial Film Council. It was evaluated as an outstanding film that contributes to the introduction of the Japanese economy and industry to the rest of the world.
Skin chromophore analysis recognized by the I S & T	A paper, "Application of Image-Based Skin Chromophore Analysis to Cosmetics," written jointly by Chiba University and Kao Corporation, received the 2005 Charles E. Ives Award (best engineering paper) sponsored by the Society for Imaging Science and Technology (IS&T). The paper was recognized for its new approach and significant contribution to applied engineering.
Nikkei Excellent Product and Service Award for 13 consecutive years	<i>Resesh</i> , fabric freshener won the 2005 Nikkei Excellent Product and Service Award and Nikkei MJ Award. This award is to commend excellent products and services that gained the lead in their specific sector and developed a new market.

Social Activities

Building Close Communication with All Stakeholders

Communicating with stakeholders through diversified media, Kao is developing together with society.



Consumers/Customers

- Kao determines consumer and customer needs to provide products and brands that bring satisfaction and joy. The products we develop are not only functionally superior and emotionally appealing, but also safe, reliable, of minimal environmental impact and easy to use, regardless of the user's age or ability. Moreover, we back them up fully with accurate product information.
- Consumers: consumer consultation service (telephone, e-mail, letter, etc.), *Relief-fureai* call service (telephone counseling for nursing care), home visits to consumer monitors, focus group
Customers (clients of chemical products and professional-use products/retailers): information exchange at business meetings, retailers' meeting, information exchange with clients, extranet



- “Kao Consumer Communication Center Activity Report,” product information on the Web site, product brochures, “Kao Corporate Profile,” industrial chemical product and professional-use product information on the Web site, “Kao Chemical Forum.”

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 opinion survey “Find,” interviews with supervisors, hotline, mental health counseling, labor-management meetings, Employees’ Welfare Committee, Health and Safety Committee, company events, “Reading of CSR Report” meeting.
- Intranet, “Te-ni-te” (in-house well being journal), “Kao Family,” “Kao Video Report,” “Kao News Quarterly.”



Suppliers

- Kao strives to be fair and transparent in all of its transactions. We work together with our business partners to enhance supply chain management while cooperating to deal with and

improve our responses to social issues such as environmental protection and human rights.

- Quality improvement meetings, regular meetings, supplier satisfaction surveys
- Guidelines for Procurement of Raw Materials, Green Procurement Guidelines.



Local Communities

- Kao’s responsibilities go beyond simply complying with laws and paying taxes. We strive for active interchange with the local communities in which we operate, giving full consideration to issues such as environmental protection and human rights. By doing so, we contribute to the development of each community as an integral member.
- Communication events with neighboring residents, local events, factory tours, exchange meetings with NPOs, support for Corporate Citizenship activities.
- Corporate Citizenship activity information on the Web site, site environmental reports (five factories).



Shareholders/Investors

- Kao maintains profitable growth through heightening the added value of products. Positioning beauty care and health care businesses as the driving force behind its growth, Kao inputs management resources in these areas. To this end, it innovates work systems and develops businesses speedily on a global basis.
- General shareholders meetings, financial results briefings, e-mail (information provision), Web inquiries.
- Investor Relations on the Web site, “Business Report,” “Annual Report,” “Business Results.”



Environment

- Kao promotes measures to counter global warming and works to realize a recycling-oriented society through its “Three Rs” initiative. In addition, we focus on appropriate management of chemical substances from raw materials to disposal.
- “Reading of the CSR Report” meeting, consumer consultation service.
- CSR Report, Approach to Environmental Issues on the Web site, “Life Information on Environment and Safety.”



Kao actively communicates with consumers and utilizes the feedback in product development and daily business activities.

Kao endeavors to develop innovative products by combining consumer needs and its unique R&D seeds. Constantly emphasizing dialogue with consumers, we are making efforts on a global basis to reflect consumer feedback in our products and business operations.

Product development from a consumer perspective

Kao nurtures a consumer-oriented corporate culture in everyday business operations in order to become a company that best knows its customers in each market.

The business divisions responsible for developing products and marketing strive to identify consumer expectations of our products by conducting in-depth consumer research. In addition, we hold focus groups and carry out home visit surveys to directly listen to consumer voices and understand their lifestyles. In this way, we try to discover potential needs that even the consumers themselves may not be aware of.

In October 2005, we incorporated the former Lifestyle Research Center and the former Business Creation Division into a new organization called Products and Lifestyle Research Center. The new Research Center aims to “quickly grasp future potential needs and changes and propose new values and lifestyles based on thorough research on ordinary citizens from people’s perspective and *Genba*-ism.” The Center studies various themes related to people’s current living conditions, including prevention of pollen fevers and tips for living with pet dogs. Research data are released both internally and externally and used to develop new products.

Improving products by using consumer feedback

In fiscal year 2005, Kao Consumer Communication Center, our direct contact point

with consumers, received a total of approximately 120,000 telephone calls, e-mails and letters, which was 97% of the number of opinions we received in the previous year. Reflecting people’s growing anxiety about the safety of paraben, nanoparticles, and asbestos, etc. following various news reports, we received a large number of inquiries about the safety of these substances. At the Kao Consumer Communications Center, we respond to each consumer’s voice in an accurate, rapid and kind manner, always from the consumer’s perspective, to ensure customer satisfaction. Additionally, we update our “Products Q&A (frequent inquiries and answers)” on our Web site to provide adequate information to consumers.

From consumer voices, we identify the issues to be tackled, and such divisions as the Consumer Products Business, the Research & Development and the Production & Engineering work together to utilize consumer feedback in product development and business operations. There are a number of cases where consumer voices have been incorporated into our business improvements, which cover a range of areas including product performance, containers, labeling, and advertising.

Consumer communications on a global basis

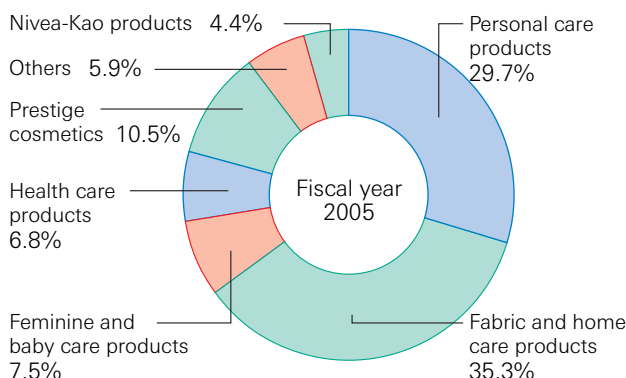
To expand our communication efforts on a global basis, we held the first Asia Consumer Communications Manager Meeting in November 2005. The conference was attended by consumer communication managers of Kao group companies in China, Hong Kong,

Taiwan, Vietnam, Thailand, Indonesia, Malaysia, Australia, and Japan. We shared information about each country’s current situation of consumer communication and held productive discussions about responding skills. As global marketing is likely to accelerate to cover more products year-by-year, it is even more necessary to continue information exchange as well as to analyze and share the consumer information collected by each country. By doing so, we intend to support brand development and improve overall consumer satisfaction levels through our responses across Asia.

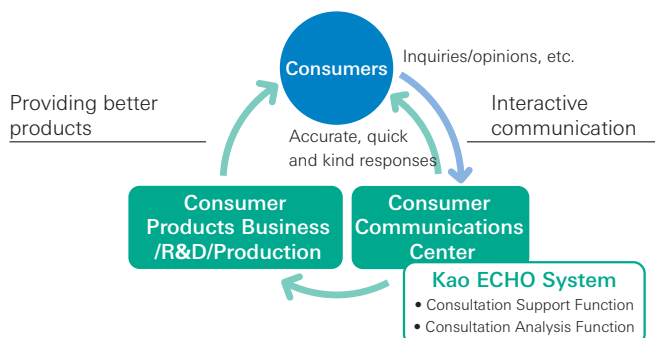
Consumer attitude/fact-finding survey concerning consumer consultation

Consumer attitudes toward products and services changes depending on the social environment. The Kao Consumer Communications Center has conducted consumer attitude surveys on its consultation services since 1987. Its aim is to understand consumer opinions objectively and determine the actual facts to use the survey results for improving and innovating our consumer consultation services. In the 2005 survey, in addition to research on consumer attitudes and viewpoints concerning daily household products, cosmetics, and health foods, we investigated gender differences in such attitudes. The results revealed that while consumers expect high quality products, they are also significantly interested in company policy and how the company meets its social responsibilities. Another finding was that men tend to have a more critical attitude towards companies than women. A summary of survey

Breakdown of Consumer Inquiries by Business Area (*including Nivea-Kao)



Mechanism to Reflect Consumer Voices in Products



results were disclosed both internally and externally via a booklet titled “A Study on the Environment Surrounding Consumers and Consumer Attitudes.”

Consumer satisfaction survey

Every year, the Kao Consumer Communications Center carries out a survey of consumers who made inquiries on their satisfaction with our responses. In fiscal year 2005, we received high ratings—more than 90% of all respondents replied “satisfied or fairly satisfied.” The launch of the sixth Kao ECHO System (consumer communications system) contributed to expediting product replacement and reporting of research results, which led to the higher ratings.

Providing appropriate information

Production of a specific product is sometimes terminated due to various reasons. We announce such information on our Web site prior to termination for the convenience of users, and introduce alternative products. If we have remaining stock of the product to be terminated, we have a system to sell these via our Web site to loyal users. They can order the products at “Kao Mail Order - Users Corner” on our Web site.

HP Users Corner

<http://www2.kao-shop.jp/fan/> (only available in Japanese)

Re-release of products to meet user requests

Production of *Refreshing Bub Shower*, which reduces the feeling of stickiness by sweat after taking a bath, was terminated in the spring of 2004 because demand was unstable. However, Japan was hit by a heat wave in the summer of 2004, and our Consumer Communications Center received a number of calls from consumers requesting re-release of that product. We found that the product had been more popular among people of all ages from children to the elderly than we had assumed. People who do not like air conditioning or suffer from heat rash are fans of this product. So we decided to re-release the product in the spring of 2005. When we mailed a letter announcing the re-release to loyal users who requested, we

got a lot of feedback from them. We confirmed that by continuing sincere communications with consumers, we can establish a relationship of mutual trust.

Awareness-building initiatives at the Consumer Communications Center

Recently, public distrust in corporate activities and concerns about food safety have increased due to the revelation of a series of scandals. Kao thinks that providing consumers with appropriate information quickly is necessary to perform corporate social responsibility as well as to earn consumer confidence and trust in Kao. As part of the efforts to increase people's awareness, consumer seminars have been held by the Consumer Communications Center. In fiscal year 2005, about 9,000 people attended 82 such seminars.

Today, a tremendous number of products are on the market to meet consumers' diversified tastes and lifestyles. At seminars, such themes as how to make washing and house cleaning more effective and efficient, and the effect of health care products to reduce body fat, etc. have been taken up. The participants commented that they now understood the differences in product features and how to better use them, or that they came to have better knowledge about food for specified health use and anti-obesity. These seminars not only contribute to promoting confidence and understanding of Kao products but also to environmental education in general. We also conduct seminars designed for persons with disabilities, who have fewer chances to get information, to help them use products more safely. In 2005, we organized a hair care workshop to meet a request by the Osaka Association of the Deaf.



Column

Product improvement based on consumer voices

Merries (small diapers for new born babies)

Home delivery service

As an increasing number of women are having lower weight babies, in 2004 Kao started a home delivery service of *Merries* diapers “small size for new born babies,” which was used exclusively by maternity hospitals. This service is welcomed by women who have lower weight babies.



HP Merries home delivery service

http://www.kao.co.jp/merries/products/hos_nbs.html (only available in Japanese)

Warning on refillable plastic package

Because refillable plastic packages have become more popular, more cases of liquid spills due to splits and holes have been reported. In February 2005, we added a warning on such packaging to avoid spills that states, “This plastic package is made of soft material. Please be careful not to damage it when carrying and storing.”



Building a cooperative system encompassing the entire supply chain

In day-to-day business operations, Kao establishes strong partnerships with customers of each business, such as chemical products, professional-use products, consumer products and prestige cosmetics. We ensure fair and transparent transactions with suppliers.

Supply chain cooperation

Kao has various groups of customers according to its different business areas, including chemical products, professional-use products, consumer products, and prestige cosmetics. Establishing close relationships with customers in each product group, we try to identify consumer needs and supply superior products. We also conduct fair and transparent transactions with the relevant suppliers.

Cooperation with customers of chemical products

Kao's chemical products, comprising oleochemicals, surfactants, and various specialties, constitute one of its core businesses. By meeting diverse customer needs through our original technologies, we provide customers with products that satisfy their requirements. To make this possible, we have to establish a strong partnership with our corporate customers. We see closely the frontline operations of corporate customers' product development and the actual sites where the relevant items are used so that we can provide high value-added products.

Using the internet and extranet, we quickly exchange information about safety regulations with our customers. Concerning the MSDS, we not only prepare Japanese and U.S./European versions but also Korean and Chinese versions to cope with global needs.

Developing products and technologies that contribute to environmental conservation is indispensable to create a sustainable society, and we are making efforts to develop such chemical products. The following are some of our major achievements in this field:

- Achieved complete elimination of chromium from catalysts used for alcohol production.
- Development of bulk-increasing agent for paper (enables reduced pulp use).
- Development of *Viscotop*, advanced special thickening agent for concrete (prevents water contamination for civil engineering).

In 2005, we implemented RC (Responsible Care) patrols at eleven major distributors to ensure environmental conservation and compliance with laws and regulations.

Developing professional-use products business

Kao Professional Services Co., Ltd. provides various businesses, including the food service industry, hotels, hospitals, and cleaning shops with a variety of products and services based on surface science and microorganism control technology that Kao has studied and developed over a long period. Through communications with customers, we determine their needs and provide both services and information, including products and also the most appropriate management methods for their usage. Recently customers' calls for

more consideration to be given to safety and the environment has been growing.

For food factories, we offer a centralized hygiene control system. This covers delivery in large reusable plastic containers, economical and safe use using accurate measuring tool, provision of special refill containers, and work standardization with illustrated manuals. In this way, we help our customers improve their hygiene, safety, and environmental management.

We continue to carry out collaborative activities with hotels. We proposed liquid soap/shampoo/conditioner dispensers to replace the traditional sachet-type amenities, and the shift to dispenser use has spread widely. This results in a reduction in waste and costs and saving of resources. We offer products not only for hotel guests but also for hotel employees. For example, we provide bathtub cleaners with high cleaning and rinse performance, which helps reduce water consumption and improves work efficiency. This cleaner is being received well.

Contributing to the growth of retailers

Aside from usual business meetings, we hold periodic meetings with retailers to share information through Kao Hanbai's nationwide network. At such meetings, we hear retailers' opinions about product sales and consumer attitudes.

In 2005, we solicited new product ideas from employees of Kao Hanbai and Kao Merchandising Service who have

Column

Development of *Viscotop*, chemical product

Viscotop is a new functional thickening agent that prevents concrete from dissolving in water. In developing *Viscotop*, we applied the technology of surfactants contained in detergents to civil engineering and construction methods, which contributes to preventing water contamination. When we talk with users working in the civil engineering and construction field, we are often surprised to find differences in technical common sense and definitions of terms

between us. Recognizing such differences, it is important to propose what Kao can do as a chemical manufacturer, identify the issues that users themselves have not noticed, stimulate needs that they thought impossible to realize, and offer relevant technologies. When we integrate users' strengths with ours and maximize them, we succeed in developing unprecedented value-added technology,



Hotaka Yamamuro
Performance Chemical
Research Laboratories

contact with retailers in their everyday operations. We received many ideas that reflect consumer needs or have high marketability, and posted the selection results on the in-house intranet, while sharing them with the Product Development division.

The retailer is an important interface between consumers and Kao. Using the information provided by retailers for the development/improvement of products and enhancement of sales activities, we are making efforts to improve consumer satisfaction levels.

Product education

Kao Hanbai sites a Product Education Center at each regional sales office to provide retailers with product information. At the center, we explain product features, their performance and usage, and the market conditions to retailers who have direct contact with consumers. This is to help retailers further expand their business by stimulating communication with consumers through better product knowledge. In fiscal year 2005, we held 1,047 seminars for retailers across the country on how to give consumers the best advice on our products.

CSR-based procurement

Suppliers are indispensable partners for Kao to conduct its business. Also, from a CSR perspective, we have to build strong partnerships with suppliers. In addition to the Green Procurement Guidelines that we have already implemented, (See page 46.) we established the Guidelines for Procurement of Raw Materials (See page 54.) in May 2005, which contain procurement policies focused on equitableness, fairness, conscience, the environment, and human rights. Currently, we are preparing the standards and doing preliminary studies in accordance with these guidelines.

Kao uses palm oil and palm kernel oil as one of the major raw materials of its oleochemical products. Concerning these oils, the Roundtable on Sustainable Palm Oil (RSPO)* is undertaking research on a global basis to explore methods of sustainable production. We confirmed that the palm oil and palm kernel oil that Kao uses is all purchased from companies that participate in RSPO or are member companies of a participant industry.

*RSPO is a private-sector group created in 2004 with the aim of discussing how palm oil should be produced from the viewpoint of sustainability.

Supplier meetings and quality improvement meetings

We try to cement the mutual trust with suppliers through satisfaction surveys, meetings, and collaborative activities.

In fiscal year 2005, 170 companies participated in the supplier meeting, where we explained the Kao Group's performance and announced our Guidelines for Procurement of Raw Materials. We also reported that we had opened helpline for suppliers to prepare for the enforcement of the Whistleblower Protection Act in April 2006. As for the raw materials used in challenging fields, we hold quality improvement meetings with suppliers. In fiscal year 2005, a total of 94 meetings took place with the participation of 44 suppliers. We discussed and confirmed the measures to address various issues in an effort to improve the quality of our raw materials.

Collaborative System between Kao Hanbai and Retailers

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

Soliciting product ideas

Retailers' staff in charge of stores and Kao Hanbai'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.



Role of Product Education Center

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.

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

Column

Cooperation through *Genba-ism*

We organize seminars on how to give consumers best advice on products in order to nurture our high value-added products. Working in cooperation with staff in the sales division, at seminars, besides description of products, we explain how to make store displays consumer-friendly so that they create a great impact on consumers. When we receive feedback from retailers saying that the seminars helped building communications with consumers, we are very happy. We work together with sales floor leaders of chain drug stores on examining and developing promotional methods tailored for specific characteristics of drug chains and their customers. We will try to stimulate feedback from frontline operations and use it to practice *Yoki-Monozukuri*.



Mizue Shibayama
Marketing Director
Kao Hanbai Co., Ltd.

We respect employee diversity and support the improvement of their abilities and personalities through their work.

Utilizing employee feedback, Kao promotes education and a corporate culture that allows every employee to improve his or her abilities through their work. Employee diversity is another aspect to which Kao attaches importance, and Kao is advancing an "Equal Partnership" (EPS) that ensures the diversity and equal opportunities to both the male and the female employees.

Kao's basic approach to human capital

The basis of developing human capital lies in the simultaneous achievement of each individual employee's and the company's growth. Our human capital development policy is to create a system in which employees' individual pursuit of achievement brings about company progress. By creating a work environment and corporate culture in which employees enjoy their work, Kao tries to integrate each employee's strengths into the overall strength of the company. Among other things, we offer company-wide training programs designed for each employee's role so that all employees can better understand The Kao Way and put it into practice. Additionally, there are training courses that put emphasis on individual initiatives to support employees' voluntary desire to learn. (Human capital /training policy, training system See page 55.)

Diverse human capital development

To create a corporate culture and an environment that offers work motivation and joy to employees, we promote EPS to maximize diverse abilities and personalities. From three perspectives, including "awareness and culture building," "institution and system," and "human capital development," Kao is actively advancing programs to promote respect for diversity, gender equality, and work-life balance.

Equal opportunity and maximizing women's capabilities

Kao has endeavored to increase work opportunities for motivated and competent women and also the overall recruitment of women. Thanks to these efforts, more women work in more diversified fields and the recruitment of women has been growing. At Kao Corporation, the percentage of women among managers was 6.0% in fiscal year 2005, up 0.6 points over the previous year. We will further promote equal opportunities for developing abilities and building careers, regardless of gender, nationality, mid-career candidates, age, etc.

Work-life balance

Since the late 1980s, Kao has taken measures to support the work-life balance of its employees. We think that in order to create a work environment that allows employees to maximize their abilities, develop their careers, and achieve good performance, we must eliminate all obstacles except their own capabilities. Therefore, while we have created systems to improve work-life balance, we also endeavor to build awareness within the company and prepare appropriate support systems. We took these initiatives to create an atmosphere in the company whereby it is completely natural that people make use of these facilities. As a result, at Kao Corporation, more than 90% of women who had a baby took maternity and child rearing leave in fiscal year 2005, and 100% of such women returned to work after their leave.

In April 2005, Kao adopted an action plan in accordance with the "Law for Measures to

Support the Development of the Next-Generation," and introduced measures such as flexible working hours and an extension to the staggered commuting period. We have continued to enhance our systems from an employee viewpoint and implement more measures than those stipulated in the law. Currently, we are working on plans to encourage male employees' participation in maternity and child rearing.

HP Major benefit package concerning maternity and child rearing and nursing

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

Employment of disabled people

We have employed disabled persons for ordinary job positions based on the policy, "we support the independence of disabled persons as members of society to create a society where all people with and without disabilities work and live together." To build awareness, we prepared and distributed our "Guidebook for the Employment of Disabled People" in April 2006 to support workplace management. In fiscal year 2005, the employment rate of disabled persons at the Kao Group in Japan was again higher than the legal rate of 1.8%.

Moreover, we have created Kao Peony Co., Ltd. to provide a job opportunity to the intellectually disabled. (In April 2006, Kao Peony was recognized as "special subsidiary" stipulated in the Law for Employment Promotion, etc. of Persons with Disabilities.)

Meanwhile, Kao's Wakayama factory has supported production activities at the Sumiya Wasa Welfare Factory, a social welfare corporation, for 13 years since its establishment. The factory was founded to support the employment of physically-disabled

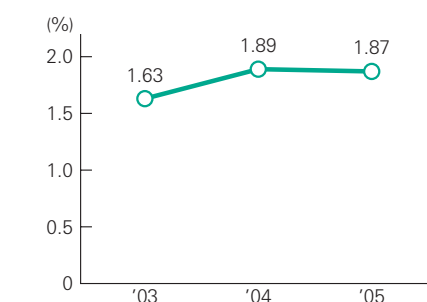
Employee Data

(Unit: persons)

		FY 2003	FY 2004	FY 2005
Permanent employees	Female	3,269	3,131	3,022
	Male	8,395	8,316	8,289
Contract employees	Female	1,713	1,989	2,194
	Male	108	94	90
New employees (permanent employees + contract employees)	Female	539	791	798
	Male	100	145	168
Employees who took maternity leave	Female	125	134	142
	Male	0	1	1
Employees who took nursing leave		5	3	2
Percentage of female managers (%)*		4.7	5.4	6.0

* Data is based on only Kao Corporation Japan.

Changes in Employment Rate of Persons with Disabilities



* Figures for each year are as of June. (fiscal year)

persons who are trying to become independent and participate in society by overcoming their disabilities.

Enhancing the re-employment system

To respond to the aging of employees and to meet the necessity of handing skills to the next generation, Kao introduced a system that allows retired employees with motivation and specialized advanced knowledge, skills, and know-how to return to work. We plan to enhance this system in the future.

Incorporating employee feedback in business operations

Employee opinion survey, “Find”

Kao has been conducting an employee opinion survey called “Find” once every two years since 2001. The survey consists of four categories: functioning of the organization, extent of dissemination of code of conduct and other policies, basic strengths, and employee satisfaction level. Respondents choose answers and can also freely express their opinions. The survey results, after disclosure to the entire company, are used to draw up an action plan at each division to improve operations. The plan is implemented at a divisional level to stimulate the organization.

The fiscal year 2005 “Find” revealed that employee satisfaction levels have continued to increase since its introduction. The results are used to identify issues that each division has to deal with, and efforts are being made to further improve operations and environment. The Kao

Group outside Japan is planning to implement this survey.

Soliciting ideas from motivated employees

We have invited employee applications for entrepreneurship since 2000 in an effort to become “a company that is attractive and appealing to people with motivation and abilities.” We invite applications for two categories—“Business Development Proposal Scheme” (venture business), and “Self-Study Proposal Scheme” (voluntary research). From this system, Customer Business (the name was later changed to the Products Emergence Department, which accepts new product development ideas, was created in 2000. Also, in 2002, the “antu Project,” which aims to improve women’s quality of life, was launched.

Emphasizing dialogues with employees

We hold labor-management meetings and have set up an employees’ welfare committee at each office and factory to enhance mutual understanding between employees and management. From fiscal year 2006, we additionally hold company-wide meetings participated in by the president and employee representatives from all offices and factories to deepen communications.

Response to the Global Compact

As Kao has participated in the U.N. Global Compact since 2005, it surveyed a total of 31 Kao overseas group companies on their compliance with the ten principle of the compact, such as items concerning human rights and labor standards. We received reports

from group companies on their compliance. They all conduct businesses in accordance with the laws and regulations of their countries, and there are no reports of child labor, forced or compulsory labor, or any other practices against the principles of Global Compact.

Column

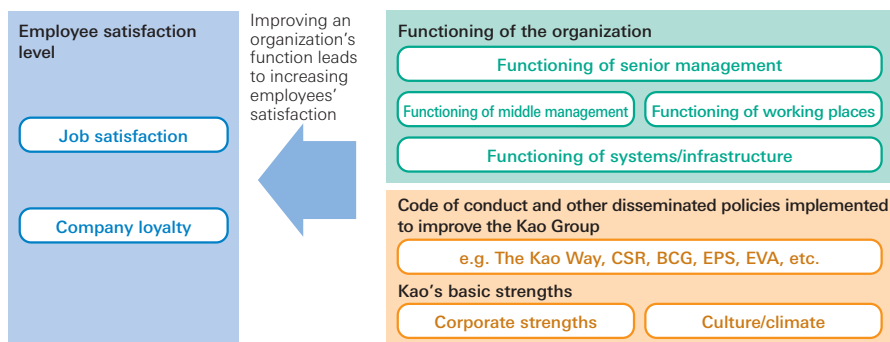
Significance of Kao Peony

By providing a workplace for disabled persons who have potential abilities but no place to work, we seek to help them become more socially independent. Persons with disabilities generally have a desire to work and feel the joy of working, and most of all, they are sincere in saying how much they enjoy working. After creating an appropriate work environment, such as facilities and equipment, if we understand each person’s ability and character and give appropriate guidance, we can improve productivity. Our current production capacity, which increased by 1.5 times compared with the beginning, is almost at the same level as an ordinary production line. We hope that persons with and without disabilities will develop their understanding of each other and grow together through the spirit of *Yoki-Monozukuri*. In cooperation with NPO for disabled persons, we hope to continue to advance the employment of persons with disabilities.



Hiroshi Iwai
Kao Peony Co., Ltd.

Composition of Questionnaire Items for “Find” employee opinion survey



HP antu Project

<http://www.kao.co.jp/antu/> (only available in Japanese)
Under this project, experienced-based seminars are held in cooperation with experts on the theme of “life, body, and mind” to help people live healthy, beautiful, and happy lives.

Kao supports employee health promotion and creates a safe working environment.

The basis of all business operations is to maintain a safe workplace and employee physical and mental health. This is Kao's stance on business, and we provide employee health promotion programs and implement occupational safety and health programs as well as disaster-prevention activities.

Kao's approach to employee health management

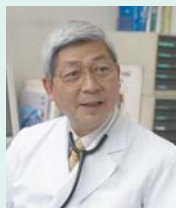
In fiscal year 2005, we launched a health program, "KAO Health 2010," to enhance the well-being of all employees. The program aims to "promote health consciousness among employees and help more employees maintain their physical and mental health."

Health advice to employees based on the results of health examinations and interviews are provided. Our health program has a system where all employees get involved in voluntarily maintaining and improving their health. In fiscal year 2003, we introduced a health support system, "Genki-Kun," which enables health interview data and health checkup results to be registered on the intranet.

Column

Health management at Kao

Before "KAO Health 2010" was launched, there were a lot of discussions among the related divisions. I really expect that "KAO Health 2010" will produce better results than the previous programs. However, it is true that although an ideal environment is available, there are some people who do not make efforts themselves. When I advise people not to drink too much or to stop smoking, some people tend to justify themselves, saying that "it cannot be helped because of work," or "I am not weak-willed enough to stop smoking." Our next objective is to ensure that this kind of person fully understands the importance of regular health checkups. It is too late to say "I should have followed the doctor's advice" after becoming ill. How to prevent people's diseases from becoming untreatable—this is one of the issues we have to deal with in the future.



Yasuo Hayashida, MD
Chief Industrial Doctor

Improving lifestyle habits

Support for improving lifestyles is one of our focus areas. Each office provides information and organizes events to improve employee lifestyles, such as nutrition education, walking and quitting smoking campaigns. We try to raise employee awareness of self care for their own health.

Mental health care

A survey by the Ministry of Health, Labour and Welfare showed that more workers are suffering from severe stress or problems at work than ever before. Kao emphasizes mental health care to ensure that employees remain healthy, not only physically, but also mentally. We have an in-house health counseling room, which accepts consultations by telephone, e-mail, and personal interviews. On-line counseling is provided quickly via the intranet. In cooperation with specialized outside organizations, we also offer telephone counseling, Internet-based consultations exclusively for Kao employees, and face-to-face counseling as part of health support programs for employees. In the internet-based consultation service, a response is made within 24 hours.

Major indices of "KAO Health 2010"

- Physical checkup results
 - BMI (body mass index; obesity measurement)
 - Blood lipids
 - Blood pressure
 - Sugar metabolism
- Interview results (lifestyle)
 - Smoking rate
 - Frequency of skipping a meal
 - Exercise (percentage of people who think they lack exercise)
 - Sleep (percentage of people who think they do not sleep well)
 - Alcohol (percentage of people who drink a significant amount of alcohol every day)
- Leave
 - Long-term leave—number of persons/days



Intranet "Health Square" (only in Japanese)

Occupational accidents and Kao's response in 2005

The number of employees who suffered from occupational accidents in the Production & Engineering and the Research & Development divisions was 24, unchanged from 2004. Among them, the number of employees suffering injuries resulting in lost work days decreased to one in 2005 from three in 2004. After accident cause analysis, it was found out that the number of accidents happened during machine operations was decreasing thanks to risk assessments for machinery and equipment. However, the accidents that occurred during manual operations didn't decrease in number. Using these analyses, we will continue risk

Programs to improve lifestyle habits

- Health education for new recruits
- Quitting smoking campaign
- Thin blood campaign
- Bone density measuring session
- Campaign to develop physical strength
- Healthy diet campaign
- Walking challenge
- Measuring of physical strength
- Yoga class

Participation rate of FY 2005 annual health checkup

- Participation rate of checkup
- 99.8%
- Follow-up rate*
- 81.0%

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

assessments of our operations.

When it comes to the entire Kao Group, including its affiliates, the number of employees who suffered from occupational accidents totaled 106, 30 of which sustained injuries resulting in lost work days. Following the previous year, we will carry out risk assessment of operations and reinforce safety education, particularly for our distribution company (Kao Logistics Service Co., Ltd.) where occupational accidents tend to occur more frequently. Since more accidents occur during operations, we have to raise the safety awareness of each worker.

On February 28, 2006, there was an explosion and fire at the plant of Fatty Chemical Malaysia (FCM), a Kao's group company, and three contract workers at a construction company suffered fatal injuries. The blast occurred during the operations of replacing pipes around the dilute methanol tank, undertaken as part of regular maintenance.

As a result of this tragedy, FCM reconfirmed safety procedures with contractors by reviewing operational specifications, etc. to prevent any reoccurrence.

Establishing an emergency contact and safety confirmation system

Since January 2005, Kao has introduced a telephone-based emergency contact and safety confirmation system to confirm employee safety in the event of a national disaster, such as a major earthquake. In November 2005, we conducted a company-wide emergency drill utilizing this system. In reviewing this drill, we identified several issues to be addressed, including safety information on the message board not posted in accordance with the rules, and condition report forms not consistent with the model. We will improve these points and plan to conduct another drill in 2006.

It is essential that we are fully prepared for a large-scale earthquake. At Sumida Office, a drill of going home on foot was conducted on the assumption that an earthquake occurs with its epicenter in Tokyo, which causes all transportation systems to stop with no immediate relief/recovery systems. A total of 83 employees participated in the drill, which also served as a health-promoting activity.

Measures for asbestos management

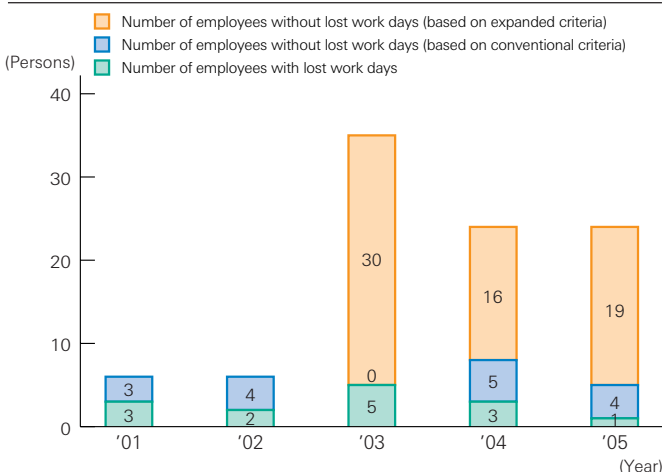
To deal with the asbestos risk highlighted

by news reports in 2005, Kao took immediate steps of examining the work environment and measuring asbestos content. We found that there were no places where workers were being exposed to asbestos fibers. We will conduct regular environmental measurement and, when removing building materials containing asbestos, comply with the "Response Guidelines for Asbestos" prepared by the Production & Engineering division.

Meanwhile, sealing materials containing asbestos—mainly used to seal high temperature pipe joints—are being removed in accordance with the replacement plan submitted to the Japan Chemical Industry Association. Replacement is scheduled to be completed by 2008.

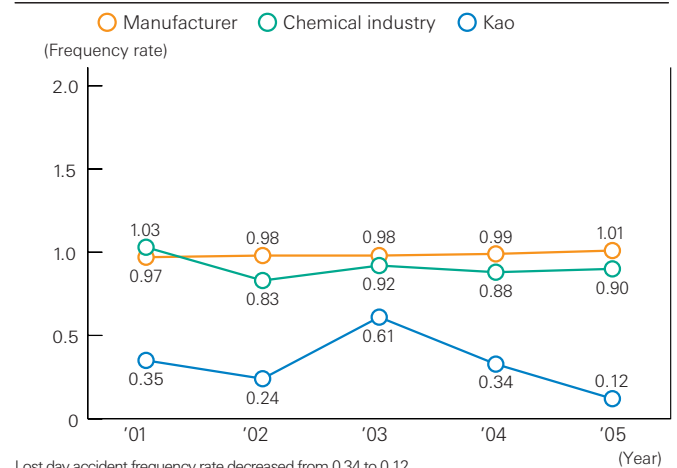
As of today, there are no consultations or inquiries about asbestos injuries to Kao's past and current employees.

Changes in the Number of Employees Injured by Occupational Accidents in the Production & Engineering and the Research & Development Divisions



In 2003, Kao expanded the criteria for defining "accidents without lost days" to include minor accidents that were not previously regarded as such.

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



Lost day accident frequency rate decreased from 0.34 to 0.12.

* Frequency rate: Numbers of deaths and injuries due to occupational accidents per million hours worked.

Kao is contributing to society under the theme of “Nurturing the Next Generation.”

To contribute to a prosperous society and its sustainable development, we are engaged in corporate citizenship activities in the following five areas, namely, the arts, environment, education, community, and promoting a barrier-free society, under the theme of fostering the next generation.

Kao's attitude toward corporate citizenship

Taking into consideration our business characteristics and the challenges that we all face today, we have been contributing to society in diverse areas under the theme of nurturing the next generation set in fiscal year 2000.

Evaluating Kao's overall corporate citizenship activities

In fiscal year 2005, an external evaluation of Kao's social commitments was carried out to review its five-year initiatives, in order to explore how to enhance our corporate citizenship.

We conducted questionnaires and interview surveys internally and externally to examine whether the following points have been appropriately achieved in all of Kao's corporate citizenship activities

based on Kao's philosophy, the Kao Way: 1) response to needs; 2) *Genba*-ism; 3) collaboration with partners; 4) maximizing Kao's resources (utilizing Kao's characteristics); 5) contributing to improving Kao's corporate image; and 6) satisfaction level of all people concerned.

The overall evaluation can be summarized as follows: 1) Kao has continued down-to-earth efforts by using its resources and achieved good results; 2) the overall theme of nurturing the next generation represents values beyond the diversity of products that Kao offers, and is suitable for a Japanese company that places emphasis on developing human resources; and 3) the theme also deals with the challenges that Japan confronts today.

On the other hand, the following were raised as points to be improved:

1) roles of Kao Corporation, the Kao

Foundation for Arts and Sciences, Kao Group companies in Japan and outside Japan are unclear; 2) commitment to local communities by Kao Group offices, plants and companies is weak; and 3) still only a small number of Kao employees participate in corporate citizenship activities.

We will strengthen our corporate support for the arts in the coming years. As a first step, we prepared and distributed the “Guide to Corporate Citizenship Activities” primarily targeting Kao Group companies outside Japan. Additionally, in order to raise Kao employees' interest in corporate citizenship activities, we will promote their understanding of the activities of the “Heart Pocket Club,” an employee-participatory donation organization.

Column

Activities of the Kao Foundation for Arts and Sciences

The Kao Foundation for Arts and Sciences, which was established to commemorate Kao's 100th year in business, marked its 15th anniversary in October 2005. In commemoration of this occasion, a booklet, *Opening the way to the future*, was published and distributed to a total of 600 universities, research institutes, and other relevant organizations. The booklet describes the history of the Foundation, which has contributed to the promotion of the arts and the development of scientific and technological research. We also held an anniversary meeting, which was attended by all the people currently involved in the Foundation. During the past 15 years, the Foundation presented grants and awards for 1,024 projects and donated 704.15 million yen to cultural and scientific projects.

HP The Kao Foundation for Arts and Sciences

<http://www.kao-foundation.or.jp/> (only available in Japanese)



Areas and Details of Kao's Principal Corporate Citizenship Activities

Area	Name of activity	Related organizations
Support for arts and culture	Supporting the Japan Association of Art Museums	The Yomiuri Shimbum Newspaper The Japan Association of Art Museums
	Supporting musical performances	Orchestral groups, etc.
	Sponsoring the Tokyo Music Competition	Tokyo Bunka Kaikan
Promotion of environmental conservation	“Creating Forests for Everyone”	The Urban Green Space Development Foundation
Support for education	Kao Teacher Fellowship	Earthwatch Japan (NPO)
	Science Experiment Classes	Kao
Support for the community	Kao Family Concerts	Kao
Promotion of a barrier-free society	Developing products that are easy to use for people with disabilities	Kao
	Providing useful information for promoting a barrier-free society	The Kyoyo-Hin Foundation
	Providing information for visually disabled persons	Braille libraries across Japan

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.

HP Corporate Citizenship

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

Exchanges between Kao People and NGO/NPO Staff

Heart Pocket Club—third debriefing session with the recipient organizations

On March 17, 2006, we held the third debriefing session with the recipient organizations of the Heart Pocket Club at Kao's Kayabacho Office.

In 2004, Kao created the Heart Pocket Club, a donation organization voluntarily joined and run by Kao employees, to provide employees with opportunities to get involved in social activities. Although it is a voluntary membership organization, about 1,500 Kao employees and directors, 10% of all employees and directors of the Kao Group companies in Japan, are members of the organization (as of the end of March 2006). Club members propose the recipient candidates, and a Steering Committee determines the recipients. Additionally, the same amounts of donations are made by Kao to some of these recipients.

Debriefing sessions are held twice a year to hear the reports by recipient NPOs and NGOs on their activities. Such reports help ensure the transparency of donations and the sessions provide employees with the chance to directly meet various stakeholders. At the third session, eight organizations out of a total of 28 recipient organizations made presentations on how they used the donations they received. After the reporting session, the organizations and Kao employees socialized to deepen the relationship. Each organization installed a booth and answered the sincere questions from employees. Such a meeting, which gives us a rare chance to meet people in completely different fields, is also welcomed by NPOs and NGOs, since it provides opportunities not only to understand what a business corporation is like but also to exchange information with other similar organizations. In the coming years, we will hold touring debriefing sessions at major Kao offices across the country.



List of recipients for fiscal year 2005 (donations to 28 recipients and disaster relief for victims of three natural disasters)

<Recipient organizations>

Carillon Child Center; ASHINAGA; Able Art Japan; Japan Braille Library; Japan International Volunteer Center; Japan Team of Young Human Power; JEN; Children Meet Artists; WWF Japan; Intervida Japan; Paramount Challenge Canoe, Wakayama Branch; Tochigi Volunteer Network; Universal Community Welfare Promotion Network; WAC Wakayama; Saitama Tennis Association for the Visually Impaired; TOYBOX; FOOTLOOSE; Mongol Partnership Institute; The 2005 World Exposition, Aichi, Japan, Youth Project-Street Children Art Festival; Peace Winds Japan; MINZOKU FORUM; People Promoting Rainwater Utilization; monetary donations to victims of Typhoon 14 in Shiiba village; Japan Wheelchair Basketball Federation; Utsunomiya City International Association; Shanti Volunteer Association; Rokkou Area Promoting Council of Forum Net Japan

<Disaster relief>

Monetary donations to victims of Typhoon 14 in Miyazaki Pref., Japan; monetary donations to victims of the Pakistan earthquake; monetary donations to victims of Hurricane Katrina in the U.S.

Support for projects, regardless of scale

Whereas global activities are of course important, I think small-scale, community-based activities are also very significant. In the two years since its establishment, the Heart Pocket Club has gradually increased its membership, and I feel that momentum is growing. Kao helped to create and operate a welfare factory 13 years ago, when the term "CSR" was still unfamiliar to most people (See page 32.). Kao has always cherished ideas for corporate citizenship, and I want to strengthen our commitment using Kao's such quality.



Hiroshi Ichino
Wasa Branch Factory
(Sumiya Welfare Factory,
social welfare corporation)
Representative of the Heart
Pocket Club Steering
Committee

Proud of supporting NGO/NPO activities

I stood for membership of the Steering Committee because I agreed with the purpose of the Heart Pocket Club and wanted to get more involved. Having a consumer perspective is indispensable in my work; therefore, it is very valuable experience to get to know different viewpoints at debriefing sessions. Each organization's activities have tremendous importance, and I feel proud that Kao supports such activities.



Takako Kuwabara
Consumer Communications
Center
Member of the Heart Pocket
Club Steering Committee

Kao proactively promotes dialogue with communities to perform its responsibilities as a corporate citizen and to help in their development.

In order to deepen people's understanding of Kao's business, we are striving to establish communications with the communities in which we operate. We have also tried to help create a sound and prosperous society through commitment to these communities.

Exchanges with communities

Developing a good relationship with the local community is important for creating a sustainable society. We are making efforts to contribute to the local community and earn the trust of people as a good community member, not only in the locations of our plants and offices in Japan, but also in all the countries where we operate businesses. Our activities span various areas, including plant tours, participation or cooperation in local events, collaboration in the activities of local economic organizations and community development, scientific education, concerts, and neighborhood cleanups. We determine specific activities taking into consideration the local characteristics and the types of operations of the respective offices.

Plant tours and classes

We conduct plant tours at all our plants across Japan. In fiscal year 2005, a total of about 28,000 people, including neighboring residents, elementary school children, junior high and high school students, university students and members of various organizations, enjoyed our plant tours. While a plant tour is a good opportunity to deepen people's understanding of our operations, we also use it as an occasion to carry out various other activities according to the production items of the plant and the local characteristics.

At the plants in Wakayama, Kashima,

Kawasaki, Tochigi, and Sakata, we also conduct plant tours that are designed to nurture the next generation. We offer science experiment classes, where participants perform chemical experiments using familiar Kao products and surfactants. These classes aim to offer participants a chance to become interested in chemistry. At plants that have a Household Products Research Laboratories or Hair Care Products Research Laboratories, experiment classes are provided by researchers.

Tochigi Plant organizes classes on sanitary napkins in which researchers give product explanation as well as conduct experiments on water-absorbing polymers. They also organize special lectures on "menstruation and health" by experts.

HP Plant tour

http://www.kao.co.jp/corp/about_kao/a06/
(only available in Japanese)

Meetings with residents living near our plants

In January 2006, Sakata Plant held a meeting with chairpersons from 11 local residents' associations. After a plant tour, we reported that we had obtained a license for industrial-waste disposal business and explained environmental measurement data. We gained the participants' understanding regarding industrial waste. At the meeting, active discussions took place, and we received questions and comments on our production. To establish a reliable

relationship with the community, we intend to continue such efforts.

Holding Kao Family Concerts

As part of contributions to the community, we hold Kao Family Concerts that are prepared and organized by our employees. The concert aims to develop love for music through experiencing musical performances by leading musicians. In October 2005, the third "Kao Family Concert in Sakata" was held as a charity concert in cooperation with the Corporate Citizenship Department. Proceeds from the concert were donated to two junior high schools in Sakata as funds to purchase musical instruments.

Activities of Wakayama Institute for Social and Economic Development

Wakayama Institute for Social and Economic Development was established in 1981 with donations from the prefecture, and various organizations and private businesses. The institute is the only think tank in Wakayama Prefecture and works to promote development of the Wakayama region. The think tank carries out comprehensive R&D in various areas concerning the economic and social issues that Wakayama faces, as well as developing innovative regional visions. By collecting and providing information, holding study groups, and proposing new policies, the institute contributes to the development of the regional economy and community, and to the revitalizations of local towns. As



Plant tour



Science experiment class



Kao Family Concert in Sakata

we have a main plant and laboratory in Wakayama City, we have been engaged in the institute's activities since 1986 as a corporate citizen. At present, one of our employees is working at the institute as a full-time researcher to help further develop the Wakayama region.

Corporate community involvement in Thailand

The spirit of community service is rooted in Thailand, a Buddhist country. Kao Industrial (Thailand) Co., Ltd. and Kao Commercial (Thailand) Co., Ltd. are contributing to the communities in a range of areas.

To support the development of science in Thailand, the companies have sponsored a scholarship program for students majoring in engineering and chemistry for almost 20 years. In fiscal year 2005, Kao provided scholarships to 15 students.

The companies also carry out the "Dreams Come True for Children" project. Kao employees directly participate in activities at a school that is chosen each year, and in the New Year, the companies use New Year cards made by children as corporate greeting cards. Employees also sell these cards and donate the proceeds to the school. In fiscal year 2005, Moo Baan Dek school (Kanchanaburi province), which was built to improve the social lives of poorer children, was chosen as the school for this project.



Kao Industrial (Thailand) Co., Ltd. and Kao Commercial (Thailand) Co., Ltd.

While this project contributes to further promoting spirit of service among Kao employees, sending a New Year card designed by children also gives Kao the chance to disseminate its social commitment to the people who receive it.

Corporate community involvement in the Philippines

In the Philippines, Pilipinas Kao, Inc. has implemented community support activities based on a policy that tries to improve the living standards of poorer people by providing programs to help them become self-supportive. Pilipinas Kao not only donates money and goods, but also been committed to the communities through education improvement in local schools from elementary to university levels, employment creation, health promotions, and environmental conservation.

In fiscal year 2005, Pilipinas Kao employees working at its Cagayan de Oro plant took part in a number of projects. They donated teaching aids and paint for repainting school buildings to local schools. They also provided medical examinations to neighboring residents in cooperation with the regional medical association, and helped manage the venue, as well as providing free medicines. Another initiative was a financial aid package to the nearby Xavier University to support their research programs.



Pilipinas Kao, Incorporated

Pilipinas Kao will continue its efforts to provide local residents with the chance to become more independent and live a better quality of life.

Charity activities in Taiwan

In Taiwan, there is a volunteer group of mothers—called "Guard Mother"—who protect elementary school children from the dangers of traffic and ensure their safety when commuting to and from school. Joining the group's activities, Kao (Taiwan) Corporation promoted the "Attack Guard Mother Charity Event" to support their initiatives. The event name is adopted from Kao's product name, *Attack*, which is also popular in Taiwan.

In fiscal year 2005, with the aim of providing safety vests to the Guard Mothers, Kao Taiwan presented about 800 reflective safety vests to mothers who walk along the roads full of heavy traffic to protect their children from traffic accidents. On April 27, 2005 a total of about 30 staff, including the president, vice president, and plant manager, joined the Guard Mothers in the school zones near the head office and factory for the day.

In order to contribute to the regional society, Kao Taiwan is also actively involved in other community activities, such as financial donations to groups protecting women from domestic violence, and to orphanages.



Kao (Taiwan) Corporation

Corporate citizenship activities in fiscal year 2005

The list below details the main corporate citizenship activities Kao has been undertaking in fiscal year 2005.

Area	Program/Campaign	Activities
Environmental conservation	"Kao Creating Forests for Everyone" Campaign	- Jan. 20, 2006: Sixth session of the "Creating Forests for Everyone" selection committee held. Total grants of 23 million yen to 39 organizations decided. - Project grants: 152 organizations applied; 31 organizations selected. Start-up grants: 27 organizations applied; 8 organizations selected.
	KIDS ISO Program	- Environmental education program for children. Donated 500 copies of a textbook to be used in school classes, and 6 staff cooperated as instructors.
Education	Kao Teacher Fellowship Overseas Field Research Program	- 50 teachers applied; 12 teachers participated (during the summer vacation in July and August 2005) - Participating projects: Hungary (nightingale), Sri Lanka (monkey), North America (salmon, orca), Vietnam (butterfly), Canada (gray whale) - Oct. 15, 2005: Debriefing session by participants held.
	Co-sponsoring the Japan Science & Engineering Challenge (JSEC2005) hosted by Asahi Shimbun	- A worldwide competition for high school students to encourage independent research in science and technology. The Kao Award given for research on breeding of the endangered lady's slipper (involving development of a support medium for culturing and an aerobic culture method based on a breeding environment survey).
	Science Experiment Classes	- July 26, 2005: Plant tour of the Wakayama Plant (28 junior high and high school students) - August 3, 2005: Fukuyama Seishikan High School, Hiroshima Prefecture - August 4, 2005: Soma High School, Fukushima Prefecture - August 4, 2005: Hachioji City Board of Education (invitation by the Board; conducted by the Consumer Communications Center) - November 10, 2005: Higashi Junior High School, Wakayama Prefecture (invitation by school)
		- During the summer and spring vacations in 2005, Service Center and Quality Assurance staff of Kao plants provided classes to local elementary school students visiting the plants. July 29: Kashima Plant; August 9: Sakata Plant; August 12 and 27: Kawasaki Plant; and July 20: Kao Vietnam Plant.
Community	Kao Family Concerts	- October 23, 2005: "Kao Family Concert in Sakata" held. The concert, entitled "Reminiscence of Audrey Hepburn," was given by violinist Ms. Kyoko Yoshida. Attended by 950 people. Revenue of 500 yen per ticket (total proceeds of about 540,000 yen) donated in full to Sakata City to support junior high school music education.
Promotion of a Barrier-Free Society	Donating Kao products to welfare facilities	- Donations made: Consumer products to 442 welfare facilities; Econa Healthy Cooking Oil to 82 NPOs providing meal services.
	Audio CD "Science in Everyday Life"	- 223 copies distributed.
Arts	The Third Tokyo Music Competition	- 277 people applied for the piano section, string section, woodwind section, brass section, and vocal section. Following the first preliminary and the second preliminary, 13 people won in the final public contest.
	Supporting the Japan Association of Art Museums	- 21 art exhibitions toured a total of 53 museums. - Five curators were dispatched overseas (from the Hokkaido Museum of Modern Art, the Fukushima Prefectural Museum of Art, the Tokyo Metropolitan Museum of Photography, the 21st Century Museum of Contemporary Art, Kanazawa, and the Fukuoka Art Museum) - Research grants awarded to four curator teams (from the Museum of Modern Art, Kamakura & Hayama, the Niigata Bandaijima Art Museum, the Museum of Modern Art, Saitama, and the Osaka Municipal Museum of Art)
		- Exhibition Catalog Award: five catalogs

Community involvement by Kao Group companies outside Japan

Kao Group companies outside Japan are also engaged in diverse activities in their local communities. The list on the right shows their major contributions in fiscal year 2005. Besides these initiatives, they are supporting communities as good corporate citizens in various ways, including cooperation/assistance in local events, donations, and volunteer programs.

Kao Group companies outside Japan	Activities
Kao (China) Holding Co., Ltd.	Provided an educational program about first menstruation at elementary schools
Kao (Taiwan) Corporation	See page 39
Kao Industrial (Thailand) Co., Ltd. Kao Commercial (Thailand) Co., Ltd.	See page 39
P.T. Kao Indonesia	Donations to the victims of the Sumatra Earthquake
Kao (Malaysia) Sdn. Bhd.	Donations to the victims of the Sumatra Earthquake
Pilipinas Kao, Incorporated	See page 39
Kao Brands Company	Donations to United Way and its volunteer activities Aid to organizations supporting women for treatment of breast cancer, prevention of domestic violence, etc. Hurricane Katrina disaster relief
Molton Brown Ltd.	Donations to disadvantaged children Disaster relief to the victims of the Sumatra Earthquake
Kao Corporation S. A. (Spain)	Provided on-the-job learning opportunities to students majoring in chemistry Supported the issuance of a community magazine
Kao Specialties Americas LLC	Donations to United Way Participated in creating flower beds at local elementary schools

Environmental Activities

From the viewpoint of the entire lifecycle of each product, Kao is promoting the development of products with less environmental burden.

Taking into consideration the full lifecycle of products, from raw material procurement to production, distribution, use and disposal, Kao is making efforts to identify the environmental impacts of its products. Through this approach, Kao aims to develop products with less environmental burden.

Kao's products and their impacts on the environment

Kao uses a large volume of vegetable oil and fat and fossil resources to manufacture products for daily consumer use. We believe that we must always pay attention to conserving resources and energy by using such resources effectively and productively at the point of production. As a company engaged in the chemical industry, we must also take into consideration the effect of chemical substances on the ecological system and human body at every stage from manufacturing to use and disposal. It is essential for us to recognize the impact of our business activities on the environment and to reduce the environmental burden as much as possible throughout the lifecycle of products in order to sustain our business operations into the future. Kao strives to

strike a good balance between business and the environment without causing any unrecoverable impact on the natural environment.

Environmental burden—our primary concerns

In light of the nature of our business, we regard the following four factors as placing a significant burden on the environment. We have set numerical objectives and placed the full weight of our efforts on reducing these burdens.

1. Greenhouse gas emissions

Production and distribution activities produce greenhouse gases such as CO₂. Kao is making efforts to reduce greenhouse gas emissions in all phases of its business activities—from research and development to sales.

2. Chemical substances management

Kao manages chemical substances using its original system, known as MI. (See page 9.) Using this system, we will promote our efforts to reduce volatile organic compounds (VOC), in addition to chemical substances subject to the PRTR law.

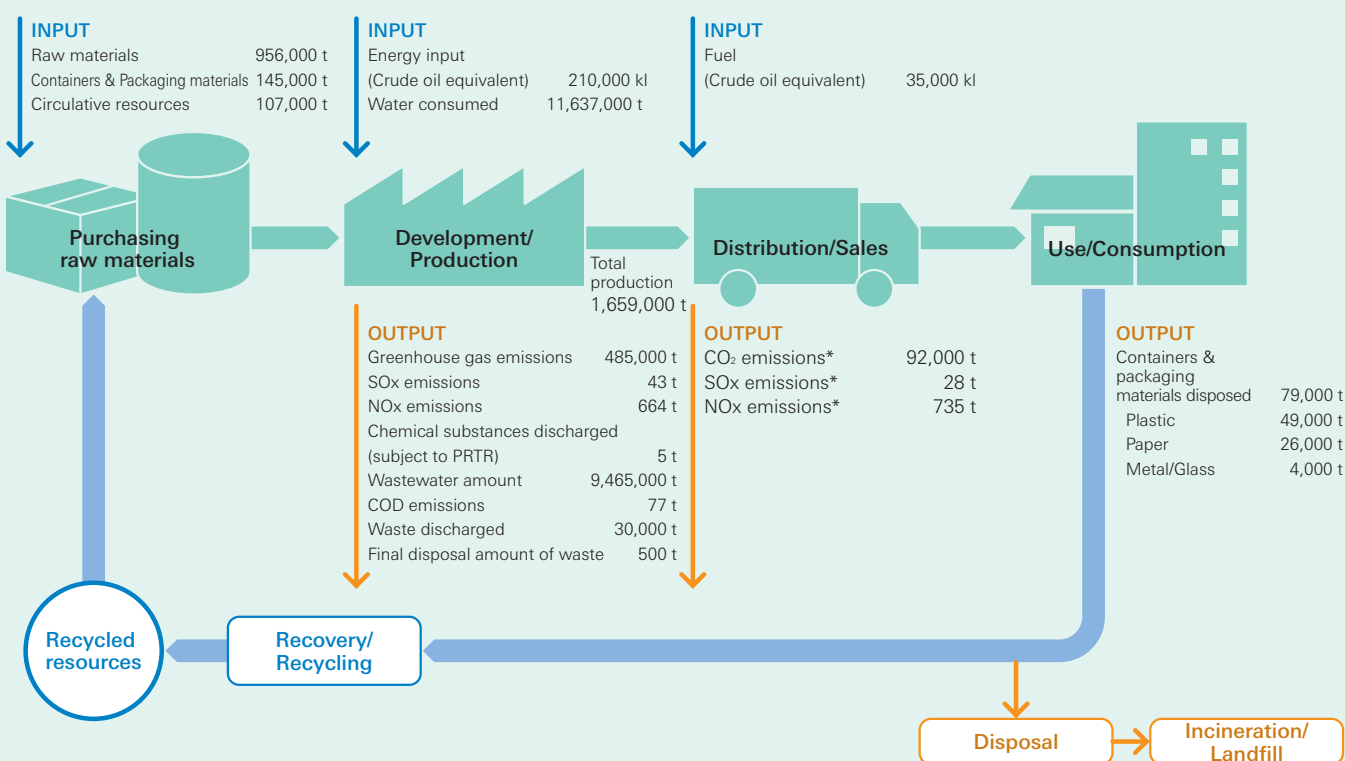
3. Industrial waste

Production process unavoidably generates by-products and waste materials, together with finished products. Kao uses such by-products and waste materials as resources as effectively as possible to minimize final disposal amounts. By fiscal year 2006, all of its domestic factories aim at achieving zero emissions.

4. Containers and packaging materials

Kao is promoting the 3Rs (Reduce, Reuse, and Recycle) for containers and packaging.

FY 2005 Lifecycle of Business Operations and Environmental Burden (See page 55 for the meanings and definitions of indices)



*: Estimated CO₂, SOx, and NOx emissions calculated from estimated transport volume of consumer products (from factory to distribution center) and chemical products

Environmental Targets and Results

In an effort to promote our environmental activities, Kao has set numerical targets for important issues. The table below shows the fiscal year 2005 results as compared to fiscal year 2010 targets.

Building on fiscal year 2005 results, we will strive for further improvement by

establishing new targets, or implementing new measures for the activities that produced insufficient achievements. Based on the national government's plan to achieve the targets stipulated in the Kyoto Protocol, Kao has consolidated efforts for global warming prevention and combined them with our energy conservation initiatives.

Kao has successfully achieved its

current targets for waste material reduction and set new numerical targets. Moreover, we are now considering targets for reducing containers and packaging.

HP Data on Environmental Burden by Plant (in Japan and Overseas)

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

Environmental Activity Targets and Results

Priority item		FY 2005 target	FY 2005 result	FY 2006 policy and target	FY 2010 target
Energy conservation		Reduce energy consumption during production activities to 76 in basic unit index as compared to 1990 level	<ul style="list-style-type: none">• Reduced to 77 in basic unit index*¹ as compared to 1990 level• Productivity deteriorated due to increased energy consumption as a result of breakdown and trial production of boilers• Promoted the improvement of operation methods and facility and equipment efficiency, etc. (199 cases of improvements)	Reinforce energy conservation activities even further and assure implementation Achieve 76 in basic unit index as compared to 1990 level	Reduce to 72 in basic unit index as compared to 1990 level
Global warming prevention		Reduce greenhouse gases* ² to 69 in basic unit index as compared to 1990 level	<ul style="list-style-type: none">• Recorded 70 in basic unit index as compared to 1990 level• The index for greenhouse gas emissions increased from the previous year due to deteriorated energy basic unit resulting from insufficient energy saving efforts despite of promoting fuel conversion• Greenhouse gas emissions were controlled by switching from private power generation to electricity purchasing	Aim at a reduction by 1% from the previous year by planning new measures for energy conservation and global warming prevention 69 in basic unit index as compared to 1990 level	Reduce to 65 in basic unit index as compared to 1990 level
Waste material reduction		All factories achieve zero emissions* ³	<ul style="list-style-type: none">• At 7 out of 8 factories in Japan and on the total basis, zero emissions achieved• Significant reduction in final disposal amounts achieved	Achieve zero emissions at all factories	The total waste from all factories will be 300 tons or less. At the same time, all factories maintain zero emissions.
Reduction of chemical substance emissions	Chemical substances subject to the PRTR law	Emission of each chemical from respective factories to be maintained at 1 ton or less	Without new emissions, the target was maintained	Maintain and continue the achievement of the target	Emission of each substance from respective factories to be 1 ton or less
	VOC* ⁴ chemicals	Complete investigations	No facilities subject to regulatory control	Emission of each chemical from respective factories to be 5 tons or less	Emission of each chemical from respective factories to be 1 ton or less
Green purchasing* ⁵		Green Purchasing Ratio for copy paper and other stationery to be 90% or higher	At 89.9%, the target was almost achieved	Continue efforts to achieve 90% or higher	100%
Green procurement* ⁶		Green Procurement Ratio to be 90% or higher	99.8%	Maintain at 90% or higher	100%

*1 Basic unit index: Amount 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: CO₂ equivalent emissions of the six greenhouse gases specified in the Kyoto Protocol.

*3 Zero emissions: To reduce the final disposal waste to 0.5% or less of the total annual waste generated in weight.

*4 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.

*5 Green purchasing: To 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.

*6 Green procurement: To purchase goods that have less impact on the environment (green goods) preferentially from environment-friendly companies at the time of purchasing goods necessary for production activities. The ratio of supplier factories that have attained a B rating or better in an environmental conservation performance assessment in the total of the factories covered by the assessment is referred to as the Green Procurement Ratio. Evaluation methods for environmental conservation performance are specified separately in the Green Procurement Guidelines.

Reducing CO₂ emissions at every phase —from product development to transport

Kao implements measures to prevent global warming in every process, from production to transport. We are also actively engaged in the development of products that facilitate the reduction of CO₂ emissions.

Efforts to prevent global warming

Kao regards global warming prevention as one of our top priority issues in our environmental activities and has taken active steps to this end. In research and development, we have promoted manufacturing practices designed to prevent global warming. Specifically, in chemical products, we have developed products that lead to the utilization of biomass.*¹ Concurrently with our efforts to reduce greenhouse gases in each process, from manufacturing to transport, Kao is calling on consumers to join in our efforts.

Efforts in research and development

All research laboratories under the Research & Development division work together with environmental studies as the theme of fundamental technology research. Environmental-conscious design, including resource and energy conservation and safety, is checked from the product development phase, using LCA and chemical substances risk assessments.

Kao reduces not only the greenhouse gases emitted directly from its factories, but also, through the promotion of biomass use, CO₂ emissions generated from the use

and consumption of its products. Kao has engaged in a variety of themes concerning global warming prevention, such as the development of highly energy-efficient processes, technology to utilize biomass carbon-neutral*², and application of biodegradable plastic made from biomass-derived materials. Results from these research programs are utilized in the development of products and new chemical substances with higher environmental safety. For example, Kao has worked on the development of a manufacturing process of functional composite powders using supercritical carbon dioxide, (See page 6.) the development of environmentally-conscious modified resin/film, and the development of pulp molding technology to produce hollow moldings.

Kao has also developed and placed on the market cleaners and other chemical products that meet the requirements of greenhouse gas emissions set by the industry. For example, in 2005 Kao developed a low temperature cleaner for the steel industry that generates a large amount of CO₂. The cleaner exhibits high cleaning performance even when the temperature of rolling oil cleansing decreased by 40°C from the previous 80°C at the time of steel plate manufacturing. Using this product enables a reduction in steam volume used for heating.

This effect is equivalent to an annual reduction of approximately 2,000 to 4,100 tons of CO₂ emissions per production line.

Efforts in production

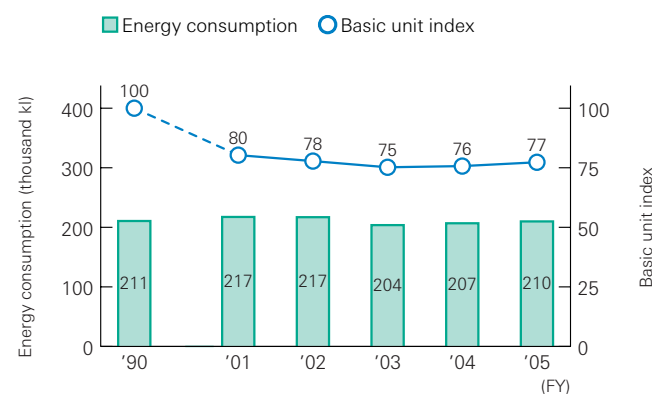
Introduction of co-generation and other energy-saving equipment

Kao has proactively installed co-generation facilities at its factories since 1991 as an energy-saving measure in production activities. Currently, a total of 20 co-generation facilities are installed in all domestic factories. In fiscal year 2005, a co-generation system was newly installed in Wakayama Plant.

Energy-saving activities in the production process

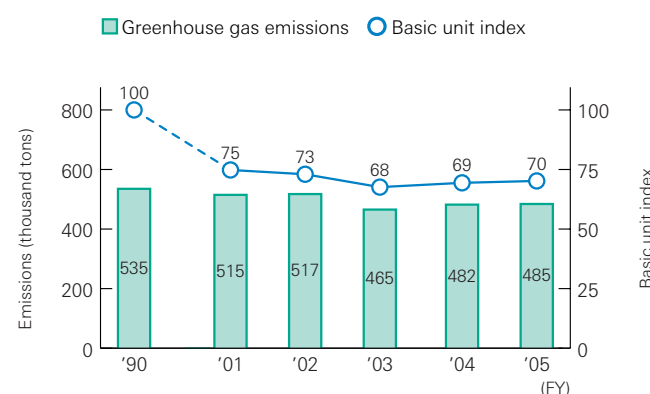
Kao achieved a reduction of 1,600 kl in crude oil equivalent as a result of the introduction of energy-saving equipment and the promotion of detailed energy-saving efforts, including rationalization and shortening of manufacturing processes. However, total energy consumption increased due to an increase in production volume. In terms of the basic unit index, energy consumption deteriorated by 1.6 points from the previous year as a result of a decrease in added value.

Changes in Energy Consumption of Production Activities



Energy consumption has been recalculated, dating back to fiscal year 1990, based on the Guidelines for Periodical Reports under Article 11 of the Law concerning the Rational Use of Energy (July 2004, Energy Efficiency and Conservation Division, Agency for Natural Resources and Energy). Waste oil is excluded.

Changes in Greenhouse Gas Emissions



Greenhouse gas emissions (CO₂ equivalent) have been calculated based on the Guidelines for Calculation Method of Greenhouse Gas Emissions Generated by Enterprises (Draft ver. 1.6; July 2003) (Global Environment Bureau, Ministry of the Environment)

Reduction in greenhouse gas emissions through fuel switching

Kao reduced CO₂ emissions by 4,700 tons from fiscal year 2004 by restraining private power generation, which uses heavy oil, and promoting the purchase of electricity with less CO₂ emissions from outside sources.

However, as a result of increased production and consequent increase in total energy consumption, greenhouse gas emissions in fiscal year 2005 increased by 3,000 tons. The basic unit index that serves as a numerical target deteriorated by 0.9 points from 2004, combined with decreased added value. In light of these results, we aim to achieve a reduction of 1% for fiscal year 2006 on a year-on-year basis by promoting a switchover to natural gas and by promoting steady grass-root campaigns at points of production. We will also explore the possibility of obtaining greenhouse gas emission rights in the future.

Efforts in office, distribution, and sales

Proactive efforts to reduce global warming

are being made not only in production facilities but also in our offices. In the distribution and sales divisions, measures to prevent global warming are implemented in cooperation with our suppliers and business partners.

Participation in the "Team Minus 6 %" campaign

Kao joined a national campaign "Team Minus 6 %" against global warming, promoted by the Ministry of the Environment since 2005. As a result, electricity consumption at offices was reduced by 825,000 kWh (approx. 2%) from fiscal year 2004. This represents a reduction of 210 kl in crude oil equivalent and that of 310 tons in CO₂.

Together with laundry finishers displayed at stores, we put signs describing "Cool Biz" and "Warm Biz," calling on consumers to join in these efforts through our products.

Efforts in distribution

The revised Energy-Saving Law obliges cargo owners to take energy-saving measures as from 2006. In accordance with this revision, Kao is reviewing the scope

and method of calculation. We are preparing to obtain data on a wider scale of our activities to promote energy-saving measures.

Column

Environmental management in Indonesia

I joined Kao Indonesia Chemicals (KIC) three years ago after majoring in chemical engineering at university. I am working in the Environment and Safety Division.

In April 2005, KIC launched a project to improve its environmental management system with the aim of acquiring ISO 14001 certification. As a project member, I have worked hard for this purpose, and KIC is scheduled to obtain ISO 14001 certification in May 2006.

KIC is a chemical company using complicated processes in its manufacturing of more than 300 types of products. There is no chemical company certified under ISO 14001 standards in Indonesia that can provide us a model for accreditation under these standards. We had a difficult time right from the first step of drafting a working plan. Moreover, there were large gaps between the actual situation and the requirements. We had to work on improving various processes in order to narrow these gaps.

I would like to contribute to the realization of an environment-friendly company by steadily improving our environmental performance in our daily operations. This should be achieved through reducing waste materials by implementing the 4Rs (Reduce, Reuse, Recycle, Recover) and continuously reviewing our processes.



Ervan Giri Basuki
PT. Kao Indonesia
Chemicals

Transportation Mode and Exhaust Gases (FY2005)

Consumer products					
Transportation mode	Work quantity ratio (%)	CO ₂ (t)	SO _x (t)	NO _x (t)	
Truck	72	71,420	23	499	
Rail (JR)	16	1,961	—	95	
Ship/boat	11	2,384	1	17	
Total	100	75,765	23	610	
Chemical products					
Transportation mode	Work quantity ratio (%)	CO ₂ (t)	SO _x (t)	NO _x (t)	
Truck	87	16,264	5	114	
Rail (JR)	9	194	—	9	
Ship/boat	5	184	0	1	
Total	100	16,641	5	124	

•Work quantity is obtained by multiplying the tonnage of products transported by the transportation distance in kilometers.

•CO₂ is calculated using the emission coefficient obtained from transport-mode-based CO₂ emission unit requirements, as defined in the Logistics Policy of the Ministry of Land, Infrastructure and Transport.

•SO_x is the sulfur content in fuel, and calculated using an emission coefficient obtained from the safety standards of the Ministry of Land, Infrastructure and Transport. (Since fiscal year 2005, emission estimates have been changed from SO₃ to SO₂.) NO_x is calculated using the emission coefficient of the Eco Program.

*1 Biomass: Renewable organic energy and resources (excluding fossil fuels) derived from living organisms. Biomass that can be used as energy includes organic matters such as wood, marine algae, kitchen refuse, paper, dead animal, fecaluria, and plankton, etc.

*2 Carbon neutral: A concept explaining part of the carbon cycle. As with fossil fuel, factories generate CO₂ when they are burned. However, they absorb CO₂ in the air through photosynthesis in their growth process. Therefore, the balance becomes zero.

Kao promotes chemical emission reductions based on an integrated management system.

To identify and reduce the risks associated with lifecycle of chemicals, Kao manages chemical substances in compliance with the PRTR Law, and issues and manages Material Safety Data Sheets (MSDS). Kao has also developed its own Comprehensive Management System for Chemicals to carry out risk assessment and management in a comprehensive manner.

Reduction of chemical substance emissions

Kao has established an integrated management structure for chemical substances based on its unique management system. We classify chemical substances into the following four classes, and these classes serve as the criteria for our chemical management.

- Prohibited chemical substances: substance that Kao prohibits usage (PCB, asbestos, etc.)
- Limited use chemical substances: substances that are being phased out (ozone layer-depleting substances, specified heavy metals, etc.)
- Chemical substances requiring careful handling: substances that must be carefully handled according to the risk profile (those specified in the PRTR Law, toxic and poisonous substances, etc.)
- Other substances: substances other than the above

Promoting green procurement

Based on the Green Procurement Guidelines established in April 2004, we have conducted an evaluation of the Environmental Management System (EMS) enforced at factories of major raw material suppliers in Japan. In fiscal year 2005, the scope of the EMS evaluation was expanded to include an

additional 109 factories and evaluations were conducted at 432 factories. The results revealed that 99.8% of the factories surveyed satisfied the guidelines. We asked those factories that failed to meet the requirements to establish an EMS and improve their operations. Currently, Kao is preparing to apply EMS evaluations to overseas raw material suppliers.

In procurement, Kao has provided its Comprehensive Management Standards for Chemicals (which specifies prohibited chemical substances, etc.) to its suppliers and asked suppliers to furnish a Certificate of Product Specification and an Information Sheet on Specific Chemicals, as appropriate. Based on information provided by the supplier, Kao confirms the supplier's compliance with the standards and decides whether or not to purchase raw materials from that company.

Chemical substance emissions from factories reduced

For the chemical substances subject to the PRTR Law, Kao achieved its mid-term target, "emission of each chemical from respective factories to be maintained at 1 ton or less." We will maintain this level in future operations.

HP Lists of Emissions of Chemical Substances Subject to the PRTR Law

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

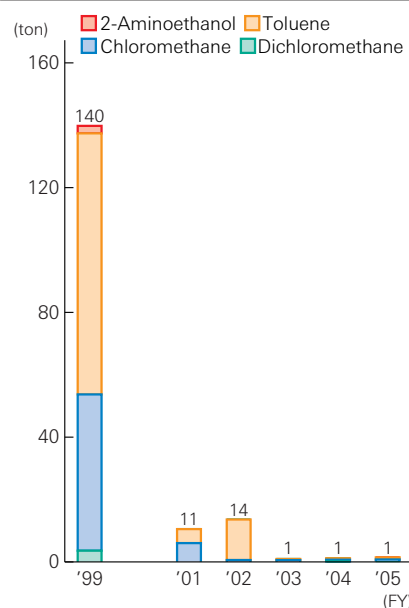
Reducing VOC emissions

Based on the revision of the Air Pollution Control Law, we conducted surveys on levels of VOCs released into the air from our facilities in 2005. As a result, no facilities were found to be subject to regulatory control. However, we voluntarily enforce VOC emission investigations to reinforce our control efforts. In line with targets aiming at "emissions of each VOC chemical from respective factories to be 1 ton or less/year in FY 2010," we will examine measures to further reduce emissions.

Providing MSDS and carrying Yellow Cards

Kao provides a Material Safety Data Sheet (MSDS) to customers when it sells chemical products. MSDS is available in Japanese, English, and other languages. The data can be viewed on the Internet at distribution centers. When chemical substances are transported by tank trucks, information about relevant emergency measures is provided to carriers. At the same time, drivers are required to carry a Yellow Card that describes all actions to be taken in the event of an emergency. For chemical substances that are transported in small quantities in drums mixed with other loads, we use a Container Yellow Card, a label attached to the container, to indicate emergency information.

Emissions into the Atmosphere of Major Chemical Substances Subject to the PRTR Law



Column

Participation in international chemical testing programs

The Organization for Economic Co-operation and Development (OECD) started a High Production Volume (HPV) Chemical-Testing Program in the beginning of 1990. This program requires that OECD member countries establish a system concerning safety information on those chemical substances of which over 1,000 tons are produced annually by that country. Kao has participated in this program since 1998. From 2000, Kao has been actively promoting this program in cooperation with other companies in the same industry, both inside and outside Japan. Kao has committed to cooperate in this program for 59 chemical materials in seven categories up to fiscal year 2004 and for an additional 49 materials in

three categories in fiscal year 2005. Kao promotes efforts to verify the safety of chemical substances in conjunction with other companies in the same industry aiming at 1) reducing unnecessary animal testings through sharing existing safety test results; and 2) producing safer products through establishing a system concerning safety information on general-purpose materials, which is a common issue. In April 2005, a program for collecting and dispatching safety information on HPV chemicals (Japan Challenge Program) was inaugurated in Japan, and Kao is also actively involved in this program. As of the end of April 2006, Kao has registered as a sponsor of the program in nine materials that account for approximately 5% of all materials covered.

Kao promotes waste material reduction through its zero emissions activities.

We are actively implementing programs to achieve zero emissions in our production activities. We make efforts for the 3Rs also in our offices (in administrative divisions) to promote the company-wide efforts for waste material reduction.

Final disposal amount of waste reduced to one-fourth

In order not only to reduce waste, but also to promote effective utilization of waste as a resource, Kao firstly considers use of waste in our production activities, and then promotes effective utilization outside the company. In fiscal year 2005, waste generation slightly increased compared with the previous year due to expanded production. However, waste treated outside the company decreased by 2,000 tons (a reduction of 6% on a year-on-year basis).

As a result of our efforts since fiscal year 2004 to achieve zero emissions, the final disposal of waste was reduced to 25% of the previous year's level. With the final disposal ratio marking 0.35% in total for all our factories, we achieved zero emissions. In fiscal year 2006, it is expected that zero emissions will be achieved in all of the factories. We will further reduce final disposal amounts, aiming at a waste generation of 300 tons or less in absolute terms.

Promoting the recycling of general waste at offices

Kayabacho and Osaka Offices are engaged in the 3Rs of general waste materials and promoting separated collection and recycling of waste resources, such as paper, plastics, and cardboard.

Distribution affiliates are also actively promoting the recycling of plastics and cardboard that became unnecessary after transport and delivery of products. In fiscal year 2005, approximately 17,000 tons of waste was recycled in total. For example, out-dated collapsible plastic containers were separated and collected in Hokkaido, Kanto, and Kyushu areas, and consigned to waste plastic recyclers to promote recycling.

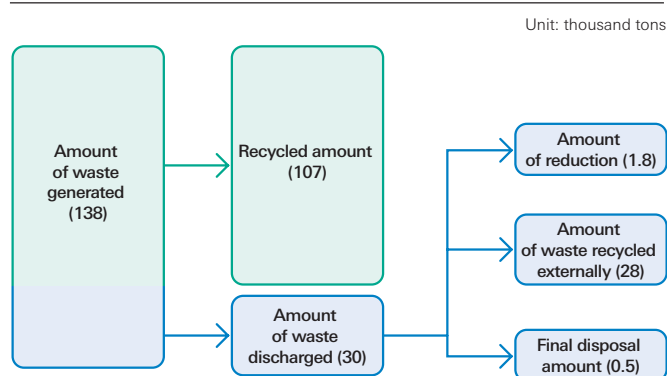
Enhancing the waste material management system

Kao established a system for sharing information on Kao's contract waste disposers and started operation of the system in September 2005 to reduce risks involving waste disposal. This

system allows us to share information concerning disposers' waste disposal licenses and the content and period of their contracts with Kao. The system is useful for ensuring optimal and efficient operations that Kao has to perform as a company that generates waste materials. In the near future, the results of audits conducted by Kao will be shared on this system.

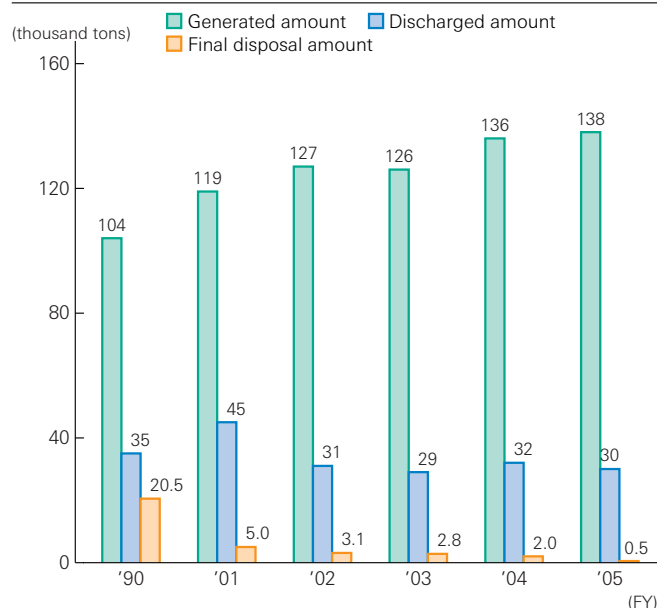
Kao is redesigning another system that has been used to manage waste materials discharged from factories so that the system can be used also at offices performing administrative tasks and domestic group companies. Completion of the system is scheduled for March 2007.

Amount of Waste Generated and Treatment Flow (FY 2005)



- 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: Resources that are reused or recycled 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 becomes usable as a resource 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



Kao actively promotes the development of products that contribute to the 3Rs in packaging.

We are committed to developing refill and replacement products and recycling containers and packaging in an effort to promote the 3Rs (Reduce, Reuse, and Recycle) of containers and packaging for the creation of a recycling-based society.

Kao's concept of effective utilization of resources

Containers and packaging become unnecessary once the contents are consumed. However, before this point, containers and packaging are part of the product, playing important roles like providing information such as directions for use and protection of product contents during distribution. From the research and development phase of products, Kao makes effort to promote the 3Rs of containers and packaging by the following approaches, in addition to efforts to ensure the required roles and functions:

- 1) Concentration of content and compacting of products (Reduce)
- 2) Reuse of containers using refill and replacement products (Reuse)
- 3) Recycling of used containers as recycled plastics/paper (Recycle)

Owing to these efforts for the 3Rs, we have succeeded in reducing the volume of materials used for containers and packaging. However, in fiscal year 2005, the amount of materials used increased by 2,000 tons over fiscal year 2004 due to the launch of new products.

Kao is currently examining a reduction target for materials used for containers and packaging based on the Japan Soap and Detergent Association's voluntary action plans.

Development of environment-friendly containers

Kao developed a paper cup molding technology to produce paper containers in any shape or form that were not available with conventional technologies. The newly developed paper containers have high heat insulation and strength equivalent to those of plastics and direct printing on paper cups is possible thanks to high surface precision. This technology has wide-ranging applications and is presently being licensed to other companies.

At the Aichi Expo 2005, the technology was used by a licensee for containers of instant miso soup that were distributed during the Kids' Eco Tour and other programs. With these containers, biodegradable materials were used also for the inner films and lids. The containers attracted people's attention at the Expo as a cup that can return to the earth, because all components of the cup can be decomposed into compost.

Efforts to reduce and reuse

Kao is also focusing its efforts on the reduction of containers and packaging materials. Thus far, we have reduced the use of materials for containers and packaging through the development of compact-type products and active releases of refills and replacement products. Also in fiscal year 2005, we

achieved a further reduction of such materials by changing the screw part of the *Wide Haiter* cap and changing the design of packaging film for *Biore-u* refills. We also reduced the use of cardboard by changing external packaging for transportation.

HP Compact-type products and compacted ratio, refills and replacement products and conversion ratio
<http://www.kao.co.jp/en/csr/report/>

Recycling efforts

In consideration of quality, cost, and the environment, Kao makes effort to use recycled paper and plastic for containers and packaging materials. For *Attack*, we use recycled paper for paper boxes and recycled polypropylene resin for measuring spoons. Recycled paper and resin are also being used in other products. Kao changed the lids for *Attack* in 2003 from plastic to recycled paper and discontinued the use of plastic handles in 2004. These changes are part of our efforts for easier separated collection of containers after consumption.

Major products in recycled paper packages

- Soap, hair coloring agents, toothpaste, bath additives, etc.

Major containers that use recycled resins

- Bottles of *Family*, dish washing detergent (PET beverage bottles)
- Bottles of *Wide Haiter*, laundry bleach (polyethylene), etc.



Biodegradable materials developed by Kao were used for the

Changes in Container and Packaging Materials used

(Unit: tons)

	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
Plastic	45,100	42,800	46,800	49,000	49,200
Paper	21,600	21,000	26,000	25,800	26,100
Cardboard	57,200	56,400	60,300	64,300	65,600
Others	3,400	3,100	3,300	3,600	3,800
Total	127,300	123,300	136,400	142,700	144,700

As a result of a review, the figures for fiscal year 2004 were changed. Increases in materials used in fiscal year 2005 are due to the release of a new deodorant.

Kao is proactively reducing the environmental impact of its production activities.

Each Kao Corporation plant, on its own initiative, consistently enhances efforts to reduce environmental impact. The factories pursue improved efficiency in distribution, contribute to reducing environmental impacts, and pay due attention to safety.

Circulatory usage of water resources

At factories, water is used in products, to clean and cool the equipment, as well as for non-industrial purposes. Kao promotes circulative water usage through efficient water utilization and purification of wastewater from cleaning equipment. In fiscal year 2005, both water consumption and wastewater amount increased slightly from the previous year. (See page 57.)

This increase was attributable to a temporary increase of well-water usage during and after summer to treat wastewater. With improvements made to the wastewater treatment method, we have managed to restrain well-water use and water consumption has now decreased. We will make sure that there will be no further temporary increases in water consumption.

Disposal of PCBs

Kao has brought together and appropriately stored polychlorinated biphenyls (PCBs) at Wakayama Plant. In 2005, two units of condensers that contained PCBs were found at Sumida Office. We immediately reported this to

the relevant government agencies and presently store the units securely at Sumida Office. In 2005, the Wakayama Plant and Sumida Office commissioned the disposal of PCBs.

Compliance with laws and response to regulations

In fiscal year 2005, there were waste gas emissions that temporarily and slightly exceeded the standard level for soot and dust at Wakayama Plant. We installed a continuous monitoring system and took measure to prevent any recurrence. We also submitted an improvement plan to the relevant department of Wakayama City Government. Also this year, BOD at the Sumida Office temporarily exceeded the sewage standards. Kao promptly strengthened monitoring and control structures and reported the incident to the sewage department of the Tokyo Metropolitan Government.

Other than the above two cases, emissions of SOx and NOx into the air and emissions of COD, phosphorous, and nitrogen into the water all met the regulatory standards. (See page 57.)

Measures for biodiversity

By promoting resource and energy conservation, waste material reduction and chemical substance management, it is possible to mitigate the impact on the natural environment and the burden on human beings and other living things. We believe that implementing Kao's current policies on the environment in our business activities is also facilitating measures to maintain biodiversity.

Kao also endeavors to practice green procurement of raw materials from suppliers all over the world and secures environment-friendly raw materials.

Moreover, Kao believes that afforestation, preservation of community forests, and support of education on these environmental initiatives are activities that also contribute to preserving biodiversity. Kao is engaged in the following activities to this end:

- Subsidies to the "Kao Creating Forests for Everyone" program (See page 40.)
- Dispatching teachers to join overseas biodiversity research projects under the "Kao Teacher Fellowship Program" (See page 40.)

Column

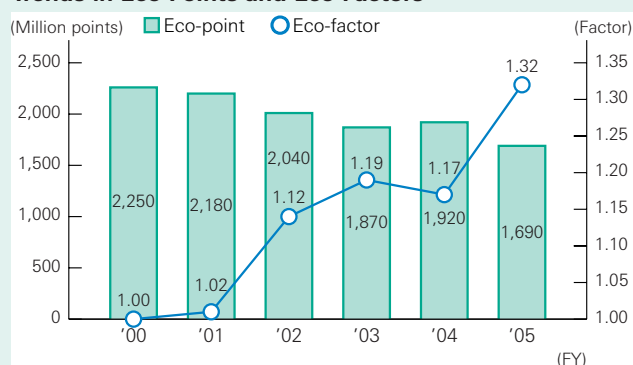
Utilization of JEPIX for environmental management index

Kao calculates eco-efficiency using the JEPIX assessment coefficient to provide self-assessment of the company's implementation levels for environmental management. Although we have not used JEPIX as a business management tool, we are currently exploring the possibility of using it for internal reference. We evaluated the company-wide environmental burden in fiscal year 2005 based on the JEPIX assessment coefficient, using a simple work sheet. The result shows that Eco-points* has significantly decreased and the Eco-factor (eco-efficiency) has improved, despite diminished added value. The main factors that have contributed to this result are the reduction of NOx and SOx due to reduced heavy oil consumption at private power generation facilities, and the significant reduction in the final disposal amount of waste.

Eco-efficiency = Value added amount (Economic indices)/Eco-point using the JEPIX method

Factor = Eco-efficiency of particular year/Eco-efficiency of 1990

Trends in Eco-Points and Eco-Factors



Calculation of Eco-points: Sum total of the respective Eco-Points by JEPIX method, calculated for core indexes of CO₂, SO_x, and NO_x emissions; amount of soot and dust emissions; final disposal amount of waste; amount of COD emissions, and amount of emissions and discharge of chemical substances subject to the PRTR Law shown in the Guidelines for Environmental Performance Indices.

* Eco-point: Represents the total environmental burden from production activities by means of a consolidated numerical value as a single index.

Kao actively promotes communication with stakeholders through its efforts for the environment.

In terms of its environmental initiatives, Kao not only dispatches information unilaterally, but also works on challenges in cooperation with various stakeholders.

Various communications through environmental initiatives

For Kao's environmental efforts, partnerships with all stakeholders are indispensable. Kao undertakes a variety of communication activities based on scientific approaches, fair and timely information disclosure, and sincere dialogues. We disclose environmental information on our Web site, in CSR reports and booklets such as "Daily Living Information on the Environment and Safety." As two-way dialogue opportunities, we hold a session for exchanging opinions during factory tours and have established consumer consultation services. We then try and incorporate feedback into our activities.

Environmental site report issued

Kao has begun to prepare site reports for each factory to help local residents and participants in factory tours understand each plant's activities for environmental conservation and safety. The reports also call for such people to make comments on our activities. In fiscal year 2005, five domestic factories issued site reports. For the Tokyo Plant, located adjacent to residential areas in the local community, site reports are also distributed to nearby residents.

Environmental report issued by Kao Corporation S.A. (Spain)

Kao Corporation S.A., operating in Spain, was certified under the Eco-Management and Audit System (EMAS) in October 2005, and issued its first environmental report in English and Spanish. (See page 15.) The

report discloses major environmental indices certified by official organizations. The report also covers internal audit systems relating to the environment and safety, the personnel administration system, training programs, and communication with local communities.

Copies of this report were distributed to major public offices and organizations, as well as to customers and business partners. Kao believes that the report is useful in informing stakeholders that Kao Corporation S.A. is an EMAS-certified company. The report will be issued every two years.

Support for Kids' ISO 14000, an environmental education program

Kao is supporting activities that help children deepen their understanding and interest in environmental preservation for the purpose of nurturing the next generation. Kao has opened an environment kid's corner on its Web site to provide environmental information for children on Kao's products. In 2005, Kao started cooperation with the "Kids' ISO 14000" environmental education program for children, which was launched by the NGO, International Art and Technology Cooperation Organization (ArTech).

Active participation in industry activities

Companies are obliged to associate through related economic organizations, trade associations, and academic societies and to cooperate in the development of such organizations. In particular, Kao believes that leading companies in each industry have social responsibilities, including playing a leading role in the promotion of the industry and the resolution of issues. From this perspective, Kao actively participates in the activities of industry associations related to chemical substances, such as those concerning consumer and industrial products. (See page 52.)

There are common challenges that face us, such as environmental conservation and safety, in attempting to realize a sustainable society. Companies are working together to

examine measures and policies concerning these issues.

The 5th Asia Soap and Detergent Association Conference was held in Tokyo in August 2005. The President of Kao Corporation attended the conference as one of representatives of the Japan Soap and Detergent Association. Participants at the conference shared their country's efforts for the environment and safety to achieve sustainable development, and information on regulatory controls. At the same time, Kao introduced detergent technologies and its response to regulatory controls.

Column

Green space of Wakayama Plant is certified as Social and Environmental Contribution Green Space - Excellent Stage 1

Wakayama Plant has 115,000 m² of green space and a part of the land is designated by Wakayama Prefecture as a historic site featuring a protective forest against storm surges, existing from the Edo period. Wakayama Plant, living up to its slogan, "the factory in the wood," is engaged in activities to preserve the forest for the protection of this historic heritage site, improving the landscape for local residents, and the creation of a space for relaxation for employees. In 2005, the green space was approved as an Social and Environmental Contribution Green Space-Excellent Stage 1 by the SEGES.* The system is designed to evaluate and approve green spaces created by companies and the activities therein and is operated by the Urban Green Space Development Foundation.



* SEGES: Social and Environmental Green Evaluation System. Documentary examinations and on site reviews are conducted for 79 items. Based on the total score in the five items of "Persistent land utilization," "Green space management," "Making full use of green space," "Vision," and "Top runner (leading company)," companies are awarded Excellent Stage 1 to 3, or Green Stage status.



FY 2004 environmental report issued by Kao Corporation, S.A.

Data

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The following information is also available at Kao's Web site.

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

- Major Benefit Packages for Maternity and Child-rearing and Nursing
- Data on Environmental Burdens by Plants in Japan and Overseas (Kao's domestic factories: 8 factories, overseas affiliated companies: 15 factories)
- Status of ISO Certification (ISO9000 series, ISO14001)
- List of Emissions Levels of Substances Subject to PRTR Law
- Compact-type Products and Compacted Rate
- Refill and Replacement Products and Conversion Rate

Kao Corporation's Offices, Plants and Research Laboratories

Offices	Kayabacho Office (Chuo-ku, Tokyo), Osaka Office (Nishi-ku, Osaka), Sumida Office (Sumida-ku, Tokyo)
Plants	Wakayama Plant (Wakayama-shi, Wakayama), Tokyo Plant (Sumida-ku, Tokyo), Sakata Plant (Sakata-shi, Yamagata), Kawasaki Plant (Kawasaki-shi, Kanagawa), Tochigi Plant (Haga-gun, Tochigi), Kashima Plant (Kamisu-shi, Ibaraki), Toyohashi Plant (Toyohashi-shi, Aichi), Ehime Sanitary Products Company, Ltd (Saijo-shi, Ehime)
Research Laboratories	Wakayama Research Laboratories (Wakayama-shi, Wakayama), Tokyo Research Laboratories (Sumida-ku, Tokyo), Tochigi Research Laboratories (Haga-gun, Tochigi)

Ehime Sanitary Products Company, Ltd is a separate company from Kao Corporation, but the company is regarded as one of Kao's factories because it is dedicated to manufacturing only Kao's products.

Major Affiliates

Japan	Kao Hanbai Co., Ltd.*1, Ehime Sanitary Products Company, Ltd.*1, Kao Cosmetics Sales Co., Ltd.*1, Kao-Quaker Co., Ltd.*1, Kao Professional Service Co., Ltd.*1, Kao Merchandizing Service Co., Ltd., Nivea-Kao Co., Ltd., Niko Seishi Co., Ltd., Inogami Co., Ltd., Kanebo Cosmetics Inc.*2, Kanebo Cosmetics Sales Co., Ltd.*2, Lissage Ltd.*2, Kanebo COSMILLION Ltd.*2, e'quipe Ltd.*2, Goldwell Japan Co., Ltd., Kao Infonetwork Co., Ltd., Kao Image Production Co., Ltd., Kao Logistics Co., Ltd., Kao Shoji Co., Ltd., Kao Peony Co., Ltd., Kao Logistics Service Co., Ltd.
China	Kao (China) Holding Co., Ltd., Kao Corporation Shanghai, Kao Commercial (Shanghai) Co., Ltd., Kao Chemical Corporation Shanghai, Zhongshan Kao Chemicals Ltd, Kao (Hong Kong) Ltd, Kao Chemicals (Hong Kong) Ltd, Kanebo Cosmetics (China) Co., Ltd.*2
Taiwan	Kao (Taiwan) Corp, Taiwan Kanebo Cosmetics Co., Ltd.*2
Indonesia	P.T. Kao Indonesia, P.T. Kao Indonesia Chemicals
Malaysia	Kao (Malaysia) Sdn. Bhd., Fatty Chemical (Malaysia) Sdn. Bhd., Kao Soap (Malaysia) Sdn. Bhd., Kao Oleochemical (Malaysia) Sdn. Bhd., Kao Plasticizer (Malaysia) Sdn. Bhd.

Philippines	Pilipinas Kao, Inc.
Singapore	Kao (Singapore) Pte. Ltd.
Thailand	Kao Consumer Products (Southeast Asia) Co., Ltd., Kao Industrial (Thailand) Co., Ltd., Kao Commercial (Thailand) Co., Ltd., Kanebo Cosmetics (Thailand) Co., Ltd.*2
Vietnam	Kao Vietnam Co., Ltd.
Australia	Kao (Australia) Marketing Pty. Ltd.
U.S.A.	Kao Brands Company, Kao Specialties Americas LLC, ADM Kao LLC, Kanebo Cosmetics U.S.A. Inc.*2
Mexico	Quimi-Kao, S.A. de C.V.
U.K.	Molton Brown Ltd*3
France	Kao Corporation (France) SARL
Germany	KPSS-Kao Professional Salon Services GmbH, Kao Chemicals GmbH
Switzerland	Kanebo Cosmetics (Europe) Ltd.*2
Spain	Kao Chemicals Europe, S.L., Kao Corporation S.A.

*1: A member of the domestic Kao Group that is included in the scope of reporting for this Report.

*2: Kanebo Cosmetics Inc. or its affiliated companies, which joined the Kao Group in January 2006.

*3: Joined the Kao Group in July 2005.

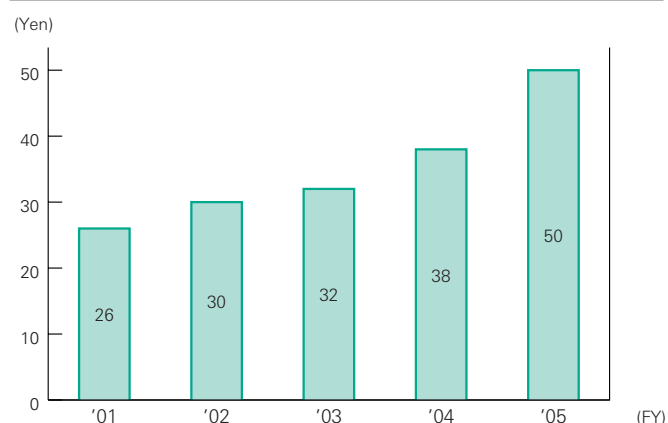
Kao's Business Fields (See page 5.)

Business Category	Sales Category	Main Products
Consumer products	Personal Care	Toilet soaps, facial washes, body cleansers, shampoos, conditioners, hair care products, hair coloring agents, bath additives, toothpastes and toothbrushes, men's cosmetics
	Fabric & Home Care	Laundry detergents, dishwashing detergents, house cleaning detergents, laundry finishers, paper cleaning products
	Feminine Care, Baby Care and Others	Sanitary napkins, disposable diapers, healthy cooking oil, tea drinks
Prestige cosmetics	Cosmetics	Prestige cosmetics, self-selection cosmetics
Chemical products	Chemical Products	Industrial edible fats and oil, fatty acids, fatty alcohols, glycerin, fatty amines, surfactants, raw polyurethanes, plasticizers for synthetic resin, toners, toner binders, aroma chemicals

Major Industrial Associations of which Kao is a member (See page 50.)

Japan Chemical Industry Association
 Japan Responsible Care Council (JRCC)
 Japan Surfactant Industry Association
 Japan Soap and Detergent Association
 Japan Food Detergent Sanitation Association
 Japan Dentifrice Manufactures Association
 Japan Hygiene Products Industry Association
 Japan Margarine Shortening & Lard Industry's Association
 Japan Bath Additive Industry Association
 Japan Cosmetic Industry Association
 Tokyo Cosmetic Industry Association
 Japan Plasticizer Industry Association

Changes in Dividend per Share (See page 21.)



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

<i>Yoki-Monozukuri</i>	Fusing Needs & Seeds Uniting Abilities <i>Yoki-Monozukuri Cycle</i>
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
<i>Genba</i> -ism	Understand the Consumer <i>Genba</i> Unification through Knowing <i>Genba</i> Inspiration from <i>Genba</i>
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

HP Full text of The Kao Way

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

Kao’s Business Conduct Guidelines (See page 22.)

Principles of Corporate Ethics

- Kao Corporation seeks to be an honest and exemplary company, guided by sensible and fair actions and driven by a fundamental adherence to ethical principles that go beyond mere compliance with laws to earn the true respect of all stakeholders.
- We shall not pursue profits at the expense of the ethical principles set out in Kao’s Business Conduct Guidelines.
- Even within a legally acceptable scope, we shall take the most exemplary initiatives.
- Illegal and unethical action is prohibited even if for the purpose of seeking to benefit the company or if following instructions from a supervisor.
- We shall not ignore illegal or unethical conduct or other such questionable conduct. Such conduct should be brought to the attention of supervisor, the Legal & Compliance Division, or other appropriate department.
- Kao shall protect and safeguard, to the maximum extent practicable, the identity of anyone who reports information regarding illegal, unethical or other questionable conduct or seeks consultation about such conduct. No unfavorable treatment shall be accorded to anyone for providing such information or seeking such consultation.
- If an employee of a Kao Group company breaches these guidelines, such employee will be subject to disciplinary actions based on the internal regulations of the company to which such employee belongs.

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

HP Full text of the Business Conduct Guidelines

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

The Ten Principles of the Global Compact (See pages 14 and 33.)

Human Rights

- Principle 1: Businesses should support and respect the protection of internationally proclaimed human rights; and
- Principle 2: make sure that they are not complicit in human right abuses.

Labor Standards

- Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;
- Principle 4: the elimination of all forms of forced and compulsory labor;
- Principle 5: the effective abolition of child labor; and
- Principle 6: the elimination of discrimination in respect of employment and occupation.

Environment

- Principle 7: Businesses should support a precautionary approach to environmental challenges;
- Principle 8: undertake initiatives to promote greater environmental responsibility; and
- Principle 9: encourage the development and diffusion of environmentally-friendly technologies.

Anti-corruption

- Principle 10: Businesses should take work against all forms of corruption, including extortion and bribery.

HP Global Compact

<http://www.unglobalcompact.org/>

Policies for Quality Management Activities (See page 10.)

1. To contribute to the wholehearted satisfaction and the enrichment of the lives of people globally, we must listen sincerely to what the consumer says about Kao products, and use the information for our business activities to improve their quality.

Consumers/customers decide on the quality of the products

2. We work unceasingly across the entire organization to improve and maintain product quality so as to encourage consumers/customers to remain loyal to our products.

Providing products that users wish to continue to use

3. Responsible for development of safe and eco-friendly products, we ensure safe usage for consumers/customers, providing appropriate information i.e. instructions regarding proper use, cautions, etc.

Ensuring safe usage for consumers/customers

4. We comply with laws and regulations at home and abroad for all business activities and fully cooperate with central/local governmental measures and international arrangements.

Legal compliance

5. We raise each individual's awareness of respective responsibility, consistently engage in fair and open business activities, and assume accountability for improved reliability.

Transparency and accountability

Guidelines for Procurement of Raw Materials (See page 31.)

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

Philosophy and Policies Regarding the Environment and Safety (See page 12.)

Philosophy Regarding the Environment and Safety

Kao is committed to a responsible approach to the environment and safety throughout the entire lifestyle 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

Improve the working environment so that employees can work in a healthy and safer environment, eradicate occupational accident, eliminate the potential risks, and maintain safe operations. Provide regular training to employees on safe work practices and in preparation for emergencies.

2. Develop products with attention to the environment and safety

Assess environment and safety aspects throughout the entire life cycle of the products, from manufacture through disposal, when developing products and technologies. Offer products with a lower environmental burden to ensure safe usage by consumers, providing appropriate information i.e. instructions regarding proper use, cautions.

3. Save resources and energy and reduce waste

To protect the global environment, develop technologies at the product design stage, which address the issues of energy and resource saving and the reduction of waste, raise productivity in terms of resources and energy, reduce waste and byproducts, and reuse and recycle resources and energy.

4. Promote human safety in the community and take a responsible approach to environmental conservation

Proactively implement environmental measures as a community member to improve safety for people in the community and conserve the environment. Solve issues that adversely influence the environment and safety responsively and without delay.

5. Comply with laws and internal controls

Comply with relevant laws and bylaws in all business activities, set and follow the Company's own code of behavior.

6. Provide adequate training

Consistently promote training on environment and safety issues to employees, raise each individual's awareness of their personal responsibility, from management to regular employees.

7. Conduct evaluations and improve credibility in the community

Conduct regular audits and self-evaluation to continuously improve activities in the PDCA cycle.

8. Disclose information and improve credibility in the community

Proactively disclose environment, and safety policies and data, and improve credibility in the community through open & bilateral communication.

RC Training Provided to Production and Engineering Division in FY2005 (See page 12.)

Name of training course	Objectives	Number of participants
Techno school	Fostering of operational engineers	17
Basic course of operation	Fostering junior factory operators	51

Results of RC Internal Audit in FY2005 (See page 19.)

	Production & Engineering	R&D, Business, Corporate	Affiliates
No. of divisions audited	8	11	3
No. of questions	423	322	61
No. of items requiring continued observation	83	29	12
Average evaluation score (5-point scale)	4.9	4.7	4.2

Kao' Ideal Employees (See page 32.)

To practice The Kao Way and achieve our corporate objectives, we aim to foster "Kao's Ideal Employees" as described below.

- 1. People with consisting challenging spirits**
They independently continue to attempt to reform existing conditions.
- 2. People with high expertise**
They have the advanced expertise necessary for their duties and roles. They have employability and are adaptable enough for environmental changes and are self-disciplined.
- 3. People with global perspective**
They have a global perspective, direct their attention to various kinds of technologies and ways of working in the world, and learn and put them into practice.
- 4. People with the team spirit to achieve superior performance**
They solicit interactive dialogue and achieve excellent results through collaboration.
- 5. People with strong ethics**
They uphold and promote ethical behavior.

Summary of Training Programs (See page 32.)

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

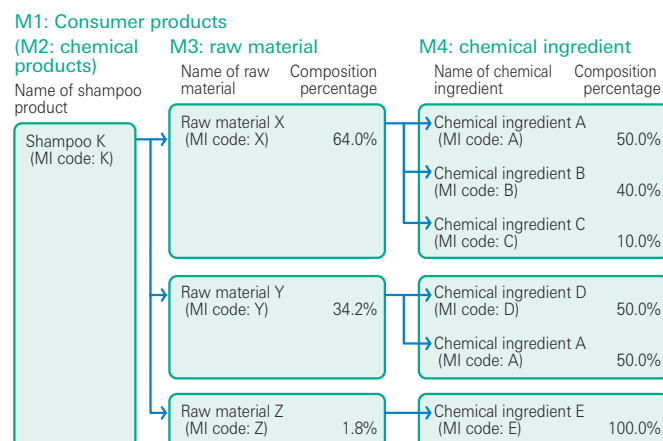
Policies Regarding Human Capital Development (HCD) Training (See page 32.)

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.

- 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.
- 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.
- 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.

Hierarchy Structure of Master Index (MI) (See page 9.)

Example of the hierarchy structure of Shampoo K that is made up of three kinds of raw materials (X, Y, Z)



By allocating MI codes for each hierarchy, our products can be managed in units of chemical ingredients.

Meanings/Definitions of Indices used in "Lifecycle of Business Operations and Environmental Burden" (See page 42.)

- Raw materials:** The amount of raw materials directly used to manufacture products (excluding packaging materials and fuel)
- Containers and packaging materials:** Total amount of cardboard, and containers and packaging materials used for products sold
- Circulative resources:** Of the waste generated from production and research activities, the amount that is recycled within Kao
- Energy input:** The amount of energy consumed in production activities (excluding energy that is used by non-production activities such as office work and research activities)
- Water consumed:** Total amount of water consumed
- Greenhouse gas emissions:** The amount of greenhouse gas emissions (six greenhouse gases as specified in the Kyoto Protocol) generated from business operations (in CO₂ equivalent)
- SO_x emissions:** Total amount of SO_x emissions from smoke and soot emitting facilities
- NO_x emissions:** Total amount of NO_x emissions from smoke and soot emitting facilities
- Chemical substances emissions:** The amount of substances subject to PRTR Law discharged into the air and water
- Wastewater amount:** Total quantity of wastewater discharged from each production plant
- COD emissions:** Figure calculated by multiplying the amount of wastewater by COD concentrations in the wastewater
- Waste discharged and final disposal amount of waste:** Of the waste discharged by production, waste sold or entrusted to waste treatment companies as waste or recyclable material, and the final disposal amount of waste
- Fuel:** Crude oil consumption calculated from the estimated amount of transported consumer products (from factories to distribution center) and chemical products
- Containers and packaging materials disposed:** The amount of containers and packaging materials used for products sold (excluding cardboard)

Method of Aggregation for FY 2005 Environmental Accounting

- 1) The method applied to this accounting complies with the Ministry of the Environment's "Environmental Accounting Guidelines 2005." It also refers to the "Environmental Accounting Guidelines for Chemical Companies (November 2003) by the Japan Chemical Industry Association.
- 2) The accounting covers Kao Corporation and its 6 domestic subsidiaries (Kao Hanbai Co., Ltd., Kao Cosmetics Sales Co., Ltd., Ehime Sanitary Products Co., Ltd., Kao-Quaker Co., Ltd., Kao Professional Service Co., Ltd. and Goldwell Japan Co., Ltd.).
- 3) The period is from April 1, 2005 to March 31, 2006.

Environmental Conservation Cost (Categories Corresponding to Business Activities)

(Unit: million yen)

Environmental Conservation Cost (categories corresponding to Business Activities)				
Categories	Key Activity and the Outcome		Investment	Cost*1
(1)Business Area Costs			2,071	3,875
Breakdown	1) Pollution Prevention Cost	Air and water pollution prevention	708	1,710
	2) Global Environmental Conservation	Energy conservation	1,026	342
	3) Resource Circulation Cost	Resource saving, waste treatment and disposal	336	1,823
(2) Upstream/Downstream Cost	Plant and equipment for environmentally-friendly products, containers and packaging recycling		15	2,744
(3) Administration Cost	Acquisition and maintenance of ISO certification, environmental publicity, tree planting within work sites		12	895
(4) R&D Cost	Environmentally-friendly R&D		224	1,970
(5) Social Activity Cost	Natural environmental conservation and tree planting activities outside work sites, donations		0	45
(6) Environmental Remediation Cost			-	0
Total			2,322	9,530

Environmental Conservation Benefit

Categories	Environmental Performance Indicators (units)	FY2004	FY2005	Change ^{*2}
Related to Resources Input into Business Activities	Energy input into production activity (crude oil equivalent, kl)	206,820	209,868	3,048
	Water consumed. (1,000 t)	11,189	11,637	448
Related to Waste or Environmental Impact Originating from Business Activities	Greenhouse gas emissions (CO ₂ equivalent: 1,000 t)	482	485	3
	SO _x emissions (t)	56	43	▲12
	NO _x emissions (t)	894	664	▲230
	Wastewater amount (1,000 t)	9,299	9,465	166
	COD emissions (t)	77	77	0
	Waste discharged (1,000 t)	32	30	▲1
	Final disposal amount of waste (1,000 t)	2	0.5	▲2
	Emissions of chemical substances subject to PRTR Law to the air (t)	5	4	▲1

Economic Benefit Associated with Environmental Conservation Activities

(Unit: million yen)

Details of Benefit	Amount ^{*3}
Revenue from sales of valuable residues	Sales value of valuable residues and fixed assets 115
Cost reduction	Reduction in costs through energy conservation 105
	Reductions in costs through resource saving 1,273
	Reduction in operation costs (maintenance costs, etc., of environmentally-friendly equipment) 182
Total	1,675

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

(Unit: million yen)

Categories	Details of Measures	Investment	Cost ^{*1}
(1) Cost related to global warming measures	Energy conservation	1,026	342
(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	71	472
(4) Cost related to noise and vibration measures	Prevention of noise	4	11
(5) Cost related to environmental conservation measures for the aquatic, ground, and geologic environments	Prevention of water pollution	634	1,227
(6) Cost related to waste product and recycling measures	Resource saving, industrial waste volume reduction, recycling	352	4,567
(7) Cost related to measures for reducing chemical risk and emissions	R&D on products and production	224	1,970
(8) Cost related to natural environmental conservation	Natural environmental conservation and tree planting activities outside work sites, donations	0	45
(9) Other costs	Acquisition and maintenance of ISO certification, environmental publicity, tree planting activities within work sites	12	895
Total		2,322	9,530

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

		FY 2003	FY 2004	FY 2005
(1) Environmental Conservation Cost	Investment (million yen)	1,839	1,987	2,322
	Cost (million yen)	9,181	9,519	9,530
(2) Environmental Performance Indicators Concerning Environmental Conservation Benefit	Energy input in production activity (crude oil equivalent, kl)	203,667	206,820	209,868
	Water consumed(1,000 t)	11,657	11,189	11,637
	Greenhouse gas emissions (CO ₂ equivalent: 1,000 t)	465	482	485
	SO _x emissions (t)	52	56	43
	NO _x emissions (t)	907	894	664
	Wastewater amount (1,000 t)	9,466	9,299	9,465
	COD emissions (t)	77	77	77
	Waste discharged (1,000 t)	29	32	30
	Final disposal amount of waste (1,000 t)	3	2	0.5
	Emissions of chemical substances subject to PRTR Law (t)	3	5	4
(3) Economic Benefit Associated with Environmental Conservation Activities	Actual benefit (million yen)	2,061	2,262	1,675

*1: Expense amounts include depreciation costs.

*2: ▲ represents a decline. The figure of "Energy input volume in production activity (crude oil equivalent, kl) in FY 2004 is different from the figure in CSR Report 2005 because an inputting error concerning the volume of electricity purchased was corrected.

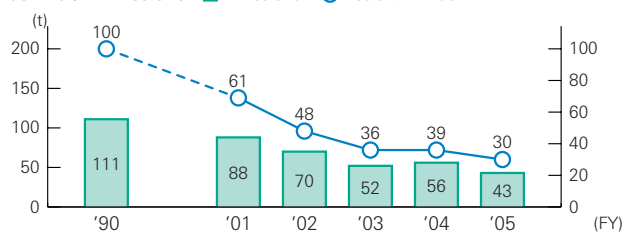
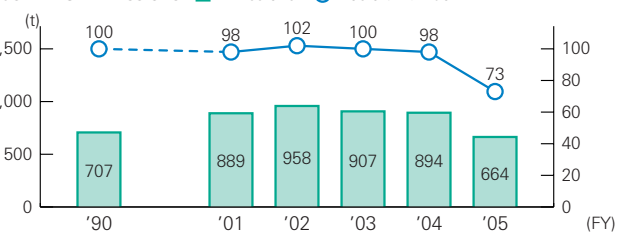
*3: The amounts of cost reduction represent annual reduction amounts of the items generated in the respective fiscal year.

- 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.

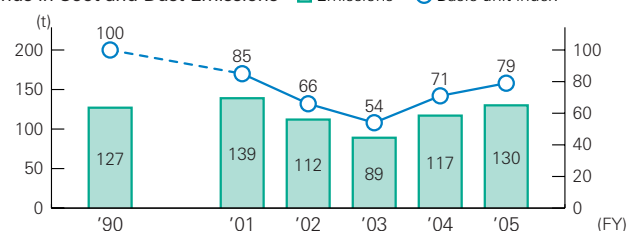
- The Guidelines by the Ministry of the Environment specify that the profit gained from the sale of valuable resources and fixed assets should be recorded. However, we recorded the sales values themselves as it is difficult to calculate the profit accurately.

- 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.

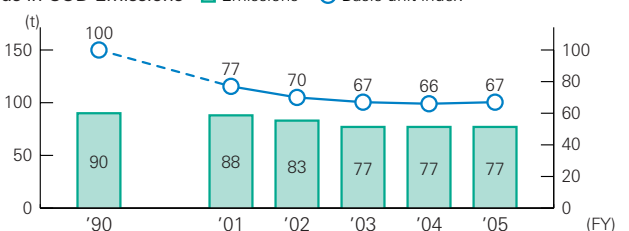
Air Pollutant Emissions, Water Pollutant Effluents, Water Consumption and Wastewater Amount (See page 49.)

Trends in SO_x Emissions ■ Emissions ○ Basic unit indexTrends in NO_x Emissions ■ Emissions ○ Basic unit index

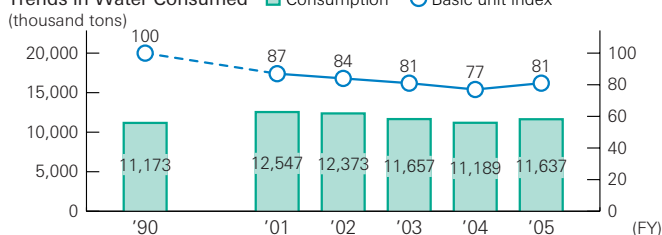
Trends in Soot and Dust Emissions ■ Emissions ○ Basic unit index



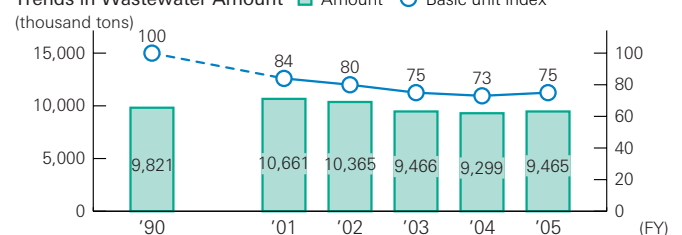
Trends in COD Emissions ■ Emissions ○ Basic unit index



Trends in Water Consumed ■ Consumption ○ Basic unit index



Trends in Wastewater Amount ■ Amount ○ Basic unit index



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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	P52, AR
EC7	Increase/decrease in retained earnings	AR
Public Sector		
EC8	Total sum of all types of taxes paid broken down by country external to the reporting organization	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	P42
EN2	Percentage of materials used that are wastes from sources external to the reporting organization	P47
Energy		
EN3	Direct energy use segmented by primary source	P42, 44
EN4	Indirect energy use	P42
Water		
EN5	Total water use	P42, 57
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	
Emissions, Effluents, and Waste		
EN8	Greenhouse gases	P42, 44
EN9	Ozone-depleting substances	Web
EN10	NOx, SOx, and other significant air emissions by type	P42, 45, 57, Web
EN11	Total amount of waste by type	P47, Web
EN12	Discharges to water by type	
EN13	Spills of chemicals, oils, and fuels	P49 (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	P48
Compliance		
EN16	Non-compliance with environmental laws and regulations	P49
EN17	Renewable energy	
Transport		
EN34	Environmental impacts of transportation used for logistical purposes	P42, 45
Overall		
EN35	Total environmental expenditures by type	P56-57

Social Performance Indicators		
Employment		
LA1	Breakdown of workforce	P32
LA2	Net employment creation and turnover	P32
LA12	Employee benefits beyond those legally mandated	P33-34
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	P35
LA6	Description of formal joint health and safety committees	P27
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 Education		
LA9	Hours of training by employee category	
LA16	Description of programs to support the continued employability of employees and to manage career endings	P32
LA17	Specific policies and programs for skills management or for lifelong learning	P32
Diversity and Opportunity		
LA10	Equal opportunity policies and programs	P32, Web
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	P53
HR2	Consideration of human rights impacts as part of investment and procurement decisions	P54
HR3	Policies and procedures to address human rights performance within the supply chain	P54
HR8	Employee training on policies and practices concerning all aspects of human rights relevant to operations	P18, 23
Non-discrimination		
HR4	Policies and procedures to prevent all forms of discrimination in operations	P53
Freedom of Association and Collective Bargaining		
HR5	Freedom of association	P18, 53
Child Labor		
HR6	Policies excluding child labor	P18, 53
Forced and Compulsory Labor		
HR7	Policies to prevent forced or compulsory labor	P18, 53
Disciplinary Practices		
HR9	Appeal practices	P22
HR10	Non-retaliation policy	P22
Community		
SO1	Policies to manage impacts on communities	
SO4	Award received relevant to social, ethical, and environmental performance	P24
Bribery and Corruption		
SO2	Policies and practices to address bribery and corruption	P53
Political Contributions		
SO3	Policies and procedures for controlling political lobbying and contributions	P53
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	P53
Customer Health and Safety		
PR1	Preserving customer health and safety	P10-11
PR4	Non-compliance with regulations concerning customer health and safety	Not applicable
PR5	Number of complaints upheld by regulatory bodies	Not applicable
PR6	Voluntary code compliance, product labels or awards received	Not applicable
Products and Services		
PR2	Product information and labeling	P10-11
PR7	Non-compliance with regulations concerning product information and labeling	Not applicable
PR8	Customer satisfaction	P28
Advertising		
PR9	Standards related to advertising	P53
Respect for privacy		
PR3	Protection of consumer privacy	P23

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.

CSR Communications through the CSR Report

Kao published its first CSR Report in fiscal 2005. Kao promotes various opportunities for communicating with stakeholders through the CSR Report so that they can gain a deeper understanding of Kao, and we can understand objectively the social responsibilities that we are expected to fulfill.

Stakeholder Dialogue

In December 2005, we held a stakeholder dialogue with the participation of NPOs and experts. That was a third meeting of this kind, since we first held the "Reading of the Environment, Safety, and Social Report" meeting in fiscal 2003. Four out of five stakeholders who participated in the meeting of this year also participated in the previous meeting. We asked for their comments on our CSR Report and exchanged views on our CSR activities.

We received the opinion that our CSR Report has been generally improved and its structure and content gives consideration to readers. In the meantime, there are still many tasks remaining, and we would like to have more communications with our stakeholders.

Time and Date: 13:30 - 16:30, Friday,
December 2, 2005
Venue: Kayabacho Office, Kao Corporation

Facilitator:
Mr. Fumitake Sakamoto
(PR Consultant, Witan Associates Limited)

Stakeholders participating:
Ms. Momoko Koga
(Representative, Fukuoka NPO Center)
Ms. Keiko Nakagawa
(Vice Executive Director, Chubu Recycling Citizens' Organization)
Mr. Shinsuke Harai
(Representative of HR LAB Ltd.)
Ms. Chieko Kikuchi
(NACS, Instructor of Sanno College)
Ms. Kyoko Inokuchi
(Editorial Department of "Kankyokaigi" and "Ningenkaigi," Sendenkaigi Co., Ltd.)

Kao staff participating:
General Manager and six members from Corporate Communications; one member from Environment and Safety; one member from Purchasing; and one member from Human Capital

Exchange of Views on CSR Activities with Employees

The Kao CSR Report 2005 was distributed to approximately 15,000 employees in our domestic group companies.

Exchange of Opinions Meeting

We held five "Reading of the Kao CSR Report" meetings as an opportunity to exchange opinions concerning CSR activities, using the Report as a communication tool. The meeting was held with the participation of employees selected from among a wide range of persons in the Production, R&D, Consumer Products Business, Sales, and Corporate divisions. Some of their comments were as follows: "Our serious and honest corporate culture is apparent in the Report"; "All the information is covered in one book"; and "I was able to understand Kao's CSR activities very clearly." Others said, "I was unable to grasp the direction of Kao's CSR activities"; and proposed "A more global perspective is necessary."

Opinions and Representative Improvements reflected on this Report

- Difficult to find the guidelines and direction that Kao values
- Public relations for Kao and reports to society in the Report are obvious, but it is difficult to see progress
- Unable to see the output of Kao's corporate citizenship activities



- Clearly demonstrate in the opening page of the report that CSR activities are the practice of The Kao Way
- Add a page which summarizes the progress in fiscal 2005
- Introduce specifically the activities of the Heart Pocket Club
- Briefly title and modulate the content for effect

In-house Questionnaire Survey

In August 2005 we conducted a survey in the form of a questionnaire, targeting all employees, in order to collect their opinions and comments. Three hundred forty-three employees answered the questionnaire, and the results were fed back within the company.

We would like to continue to review our CSR activities and actively promote communications with employees through our CSR Report in the future.



Stakeholder Dialogue



In-house Exchange of Opinions Meeting

Independent Review Report

(TRANSLATION)

Independent Review Report

June 12th, 2006

Mr. Motoki Ozaki,
President and CEO, Kao Corporation

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

1. Subject and Objective of Review

We have performed a review of certain significant information stated in the "CSR Report 2006" ("CSR Report") prepared by Kao Corporation ("Company"). The purpose of our review was to provide conclusions from an independent standpoint about whether such information in the "CSR Report" was accurately measured and calculated in accordance with calculation methods, etc. adopted by the Company with reference to Environmental Reporting Guidelines 2003 (issued by the Japanese Ministry of Environment) and GRI 2002 Sustainability Reporting Guidelines.

2. Responsibility of Management and Persons Reviewing the CSR Report

The "CSR Report" is the responsibility of the Company's management. Our responsibility is to provide our conclusions with respect to the CSR Report from an independent standpoint.

3. Summary of Review

To obtain an adequate and valid standard of basis for providing limited assurance with respect to our provided 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), Proposed Environmental Report Review Standard (issued by the Japanese Ministry of Environment in March 2004) and Environmental Information Review Practices Guidance (issued by The Japanese Association of Assurance Organizations for Environmental Information in January 2006).

4. Conclusions

With respect to the significant information stated in "CSR Report", our review did not identify items which were acknowledged to not be accurately measured or calculated in accordance with calculation methods, etc. adopted by the Company with reference to Environmental Reporting Guidelines 2003 (issued by the Japanese Ministry of Environment) and GRI 2002 Sustainability Reporting Guidelines.

5. Special Interests

There are no interests between the Company and Tohmatsu Environmental Research Institute Ltd. or its engagement personnel, requiring disclosure based on the rules of The Japanese Association of Assurance Organizations for Environmental Information.

Supplementary Explanation on the Procedure for Preparation of the Independent Review Report

Step 1

Review plan development

Confirmation of the items to be included in the report
(1) Scope of information
(2) Information collection process
(3) Information collection method
(4) Identifying the level of importance of individual pieces of information
Decision on the items to be reviewed and review methods

Step 2

Review execution

Inspection of offices and responsible managers in charge
Visit business establishments

Step 3

Review reporting

Reporting on issues (corrective actions and suggestions) identified through the review

Step 4

Final version report check

Follow up on the issues identified in Step 3

Step 5

Independent review report submission

Submission of the independent review report

Supplementary explanation concerning establishments inspected

- The auditors visited the following establishments during the review:
 - Kayabacho Head Office
 - Wakayama Plant
 - Toyohashi Plant
- 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.



On Completing the Independent Review

This year again, our Institute performed the review of the Kao CSR Report. In the following section, we would like to highlight several things that we noticed during the review process, as well as necessary points for further improvement in the future. These comments should not be considered as a part of the Independent Review Report, and do not provide any sort of assurance.

1. “Kanchan” (The Environmental and Safety Data Management System)

It seemed that the operation of the “Kanchan” system was firmly established within the company and that data was managed efficiently.

Regarding operation of the system, however, although the company has defined procedures, it is people who actually operate the system. Therefore, so that the system can be operated in the same way if the persons in charge change, it is necessary to establish a mechanism through education, internal auditing, etc., whereby operation of the system can be ensured.

In addition, as future tasks, we expect the Kao Corporation to promote efforts in order to further expand the scope of data collection and finally be able to manage data of the consolidated companies as a whole.

2. Compliance System

Just like last year, BOD (biochemical oxygen demand) exceeded sewage standards at the Sumida Office.

Since this has happened in two consecutive years, and from the perspective of risk management, Kao Corporation is recommended to consider effective rules to prevent the recurrence of this problem. In addition, we recommend that other factories also reconfirm the relevant rules and recheck whether appropriate preventive measures are in place.

3. Environmental Accounting

We confirmed that the internal rules were being adequately operated. In the meantime, there were sections in which insufficient data had been collected. We recommend that improvements to enable more efficient data collection be considered.

4. Objectives of CSR

Two years have passed since the CSR promotion system was established. In the future, it will be necessary to establish and disclose clear objectives to which Kao Corporation is committed.

We expect that in the future, Kao Corporation will continue to implement improvements and aim to improve CSR through certain and effective operations.

Tohatsu Environmental Research
Institute Ltd.

Receipt of the Independent Review

We believe that it is the foundation for CSR activities to review our daily activities not only within the company, but also from the perspective of an outsider, and then to improve them.

The independent review is to assure the accuracy of the information provided in the CSR Report from the standpoint of an outsider, and we think that the third-party review is also a means to check our way of doing businesses itself. In this year's review, there were problems, such as “we could not show the required evidence immediately,” or “our explanation was difficult to understand.” We will endeavor to solve these problems by further promoting cooperation between divisions and the sharing of information within the company.

We also understand that it is a big challenge to collect global data, establish global objectives, and promote supply-chain development.

For Kao Corporation, CSR is to conduct *Yoki-Monozukuri* based on The Kao Way, and contribute to enriching the lives of people globally. The preparation of the CSR Report is also a part of *Yoki-Monozukuri*. We will continue to practice The Kao Way step by step in the future.

Takashi Ishii
Vice President
CSR Department
Corporate Communication

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 2006

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.



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

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We promote green purchasing
for printing services.

