

Forward thinking

**BAE SYSTEMS**

REAL PERFORMANCE. REAL ADVANTAGE.

# An overview of BAE Systems: The quick read



## Why BAE Systems exists:

BAE Systems aims to deliver sustainable growth in shareholder value by being the premier global defence and aerospace company.

Defence is both legal and necessary. The first responsibility of any government is to ensure national security. This provides stability for sustainable economic and social development. The fundamental role of the defence industry is to support governments in providing national security to protect its citizens.

Human nature creates conflict, not the defence industry. It is naïve to think that there would be no more conflict if the defence industry did not exist. We all live with a constant threat of terrorism, violence and war and we in the defence industry have to confront and tackle these issues. Equally, we have to face up to the responsibilities associated with our industry. We fully recognise the role and potential use of our products and do our utmost to ensure that we deal with all our responsibilities as part of everyday business.

**US defense contractors may see boom continue.**

Green thinking

**Globalisation putting many unlikely sectors in the line of fire**

Human rights issues around the world are now beginning that lay the groundwork for the remaining companies that industry becomes increasingly global, its exposure to such. This is the case for many companies which very fine bu

**Thinking bigger & better**

Social enterprise is far more than just small community projects, it is an important model for running big businesses and public services.

Should some large companies, such as those involved with water and energy not be social enterprises? By the same token those who are running social enterprises should also aspire to be able to run large corporate

**BAE Systems to be strengthened by UK defence programmes**

Better than expected growth in revenues and earnings in the first half of the year have been announced

The Eurofighter programme has been largely responsible for this improvement in the UK programmes side of the business. The project gained momentum last year when the

## What BAE Systems stands for:

We are proud to be part of the defence industry and see our role as providing national security and protection for sovereign governments while delivering to our investors. We recognise the serious nature of our business and know that we must operate at the highest level of responsibility.

- We recognise our responsibilities to the people we employ, our customers and suppliers, our shareholders, the wider community and the environment.
- We are an ethical company and will demonstrate the highest standards of integrity and responsible management. We do not tolerate unethical behaviour or illegal conduct.
- We establish compliance with the law as a minimum and aim for higher standards where practical.
- We aim to act as a leader in our industry and be a benchmark for standards and high ethical values across the industry.
- We aim to make sure people understand the difference between a responsible defence company and the illegal arms trade.
- We take our role as a global company seriously and will contribute to the resolution of issues that impact beyond our own boundaries.

## How BAE Systems does business:

BAE Systems is a global defence and aerospace company providing a full range of products and services for air, land and naval forces, as well as advanced electronics, information technology solutions and customer support services.

We are working with customers to optimise current and future military capability across land, sea and air by providing the most efficient support and service throughout the life of our products.

We are owned by our shareholders. We aim to create sustainable shareholder value by being the premier global defence and aerospace company. Underpinning this are our company values:

**High Performance** – we will set targets to be the best, continually challenging and improving the way we do things, both as individuals and as members of our teams.

**Customers** – our priority to all our customers, both internal and external, is to understand their needs and expectations and deliver on our commitments.

**People** – all our people will follow our principles of Accountability, Honesty, Integrity, Openness and Respect and will be encouraged to realise their full potential as valued members of our team.

**Partnering** – we will strive to be the partner of choice, respected by everyone for our co-operation, integrity and openness.

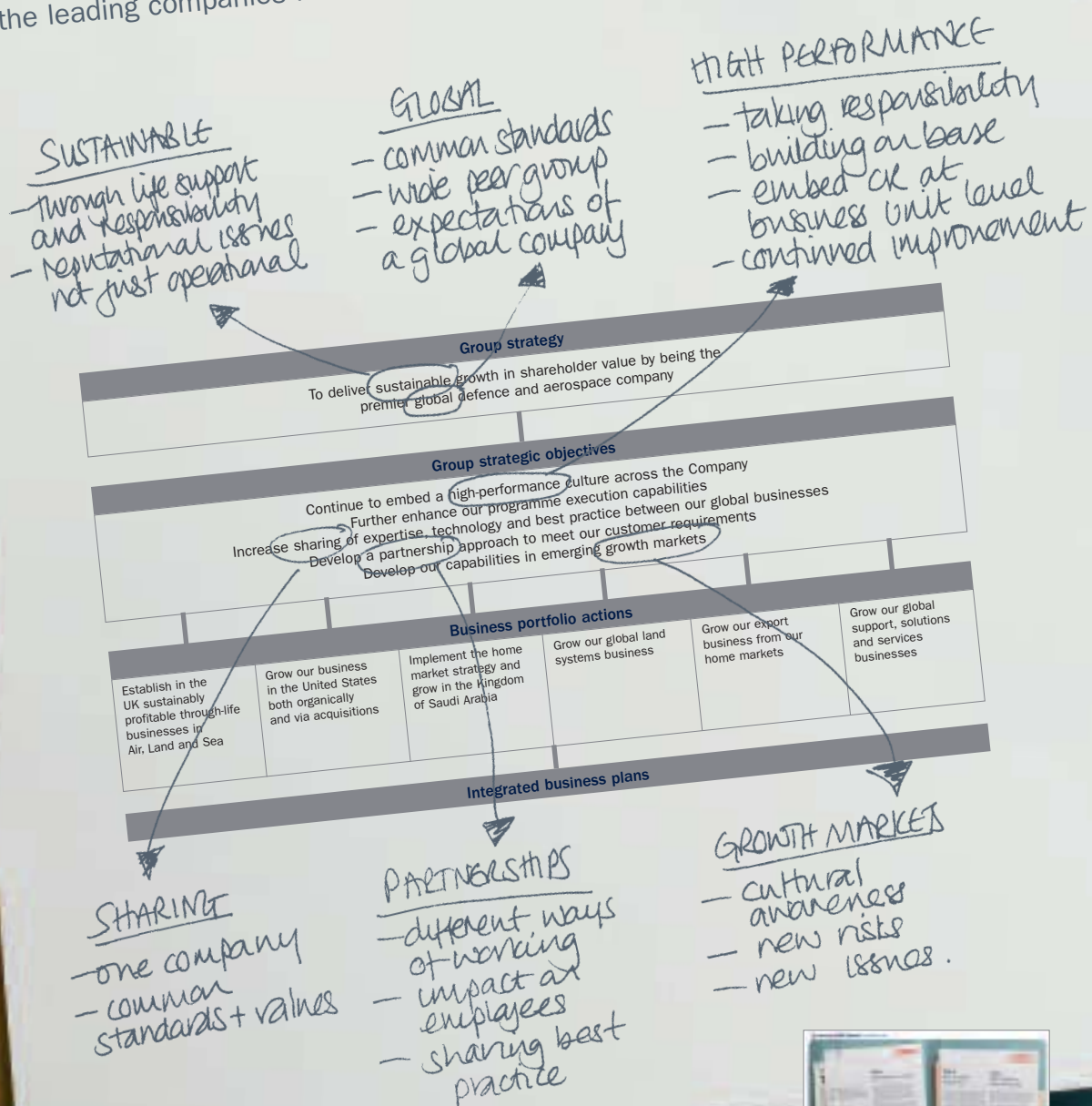
**Innovation and technology** – we will encourage the development and implementation of new ideas, new technologies and new ways of working, to secure sustained competitive advantage for our company.

# Forward thinking

Our Group Strategy is 'To deliver sustainable growth in shareholder value by being the premier global defence and aerospace company'. This requires us to take a leadership role within our industry and to perform on a par with the leading companies in other sectors.

We are developing a Corporate Responsibility (CR) agenda for the company to support our business interests and the delivery of our strategy over the next five years. This will be based on an assessment of stakeholder expectations, taking into account the CR issues particular to the defence industry and recognising that the company will also be judged against peer companies in other sectors.

The key aspects of our Group Strategy with implications for our CR agenda are highlighted below. This is developed further on pages six and seven of this report.



See overleaf for an overview of our business today ▶

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# Delivering on our objectives

**BAE Systems is first and foremost a defence company. It is also a large employer, with a significant presence in a number of communities across our home markets, a key supplier to our customers and a major engineering manufacturer. Whilst each of these aspects defines responsibilities, it is the industry we are in and the nature of our products which drives a significant part of our CR agenda.**

One of the key aspects on which we will continue to accept no compromise is compliance with our ethical business principles and policies. During 2006 we developed, piloted and rolled out across the UK business an ethics awareness training course. We do not doubt our employees but we want to ensure that they are aware of the fundamental importance that this issue has for our business. Our US business already has a similar programme in place and we will be extending the training across Sweden, South Africa, Saudi Arabia and Australia during 2007.

The safety of our employees and those working on our sites is of paramount importance and we continue to drive improvements through the setting of objectives, training and awareness and partnership with key groups. In 2006 we made substantial progress on raising the level of safety standards through an active and voluntary partnership with the Trade Unions and the UK Health & Safety Executive. We are pleased to stand up and be counted on such issues and look forward to continuing the partnership and improvements over the coming year.

The 2007 objectives of our leadership group include specific focus on ethics and safety.

Another aspect to which we are committed is the development of diversity improvement plans appropriate to each area of the business. This is necessary to support the increasingly global nature of our activities and deliver on the broader and changing requirements for capability in the future. This is a long term issue but we recognise the value and challenge that different cultures, backgrounds and approaches can bring to our business where innovation is key.

In 2002 when we first reported externally on our CR activities, our CR agenda reflected existing activity and was somewhat reactive in nature. We have progressed to a point where our CR agenda is more proactive.

To realise value from our future CR agenda it must support our business interests and be aligned to our Group Strategy. The primary objective of our strategy is for BAE Systems to deliver sustainable growth in shareholder value by being the premier global defence and aerospace company. The implications of this for our CR agenda are explained on page six of this report.

A key aspect of our aspiration to be a global company is that our peer group will no longer just be the defence sector and we will be compared to other leading companies. We will drive our CR agenda accordingly, always recognising that the CR agenda must be aligned and be appropriate to the specific issues and nature of our business.

We recognise that ours is a controversial industry and respect the rights of individuals to have differing opinions to our own. But we often find that opinions are not based on a full understanding of the issues. Through

a programme of engagement with serious stakeholders on our CR agenda and through this report we aim to better inform and provide a basis for intelligent discussion and debate.

Our employees are proud to work for our company, proud of our products and I am proud to lead it. We will continue to deliver high performance in all aspects and are committed to the continued development of a CR agenda which reflects and supports a leading global company.



**Mike Turner**  
Chief Executive



**‘ We will continue to deliver high performance in all aspects and are committed to the continued development of a CR agenda which reflects and supports a leading global company.’**

**Mike Turner**  
Chief Executive

2006 Objectives	What we achieved	2007 Objectives
<p><b>1. Workplace</b></p> <ul style="list-style-type: none"> <li>– Resolve 75% of employee grievances in the UK at local level.</li> <li>– Reflect gender diversity on leading university courses in choice of graduate trainees through a focused recruitment plan.</li> </ul>	<ul style="list-style-type: none"> <li>– 97% of employee grievances in the UK were resolved at a local level during 2006. Only one complaint required a corporate level investigation under the Group’s Respect at Work policy.</li> <li>– We met our targets to recruit at least an equal proportion of female graduates to that seeking a career in engineering. In 2006 11.2% of UK and 20% of US engineering graduates were women. Over the year, 12% of our UK and 20% of our US engineering graduate recruits were women.</li> </ul>	<ul style="list-style-type: none"> <li>– 85% of employee grievances under the UK ‘Respect at Work’ policy to be resolved through local discussion without proceeding to the corporate process for formal investigation.</li> <li>– In each of the home markets, move towards establishing a workforce reflective of the national average in terms of gender mix and ethnic diversity, taking into account variations by region and industrial sector.</li> </ul>
<p><b>2. Safety, Health and Environment (SHE)</b></p> <ul style="list-style-type: none"> <li>– Exceed safety performance commitments made to the UK Health and Safety Executive.</li> <li>– Meet our safety, health and environment targets (performance improvement criteria appropriate to risk established at global business unit level).</li> </ul>	<ul style="list-style-type: none"> <li>– Targets were set against individual business issues and all businesses included Safety, Health and Environment in their quarterly management reviews. The overall performance on safety reflects the good performance against these targets.</li> <li>– The commitments made as part of the UK Government’s ‘Revitalising Health &amp; Safety’ initiative have been exceeded – that is – we have already met targets for performance by 2010.</li> </ul>	<p>2007 SHE metrics to improve relative to 2006:</p> <ul style="list-style-type: none"> <li>– Establish, where practical, appropriate industry benchmarks for each line of business to monitor performance and establish targets to move towards best in class.</li> <li>– Group performance (Lost Days metric) to be better than relevant industry average.</li> <li>– Continue to achieve an improvement year on year in injuries/lost working time.</li> </ul>
<p><b>3. Ethics</b></p> <ul style="list-style-type: none"> <li>– Meet standards defined in our internal assurance statement.</li> <li>– Develop, pilot and roll out ethics awareness training to all employees in the UK and Australia.</li> </ul>	<ul style="list-style-type: none"> <li>– By the end of 2006 80% of UK employees had successfully completed the training. Plans are in place to ensure the remaining 20% complete the training early in 2007.</li> <li>– We also intend to roll out the training to our employees in Australia, South Africa, Saudi Arabia and Sweden.</li> </ul>	<ul style="list-style-type: none"> <li>– Initial ethics awareness training to be completed by new starters within one month of joining.</li> <li>– Initial ethics awareness training to be implemented within three months of completion date for any acquisition.</li> <li>– Survey to be undertaken to evaluate effectiveness of 2006 UK ethics awareness training package. Implement agreed corrective actions in 2007.</li> </ul>

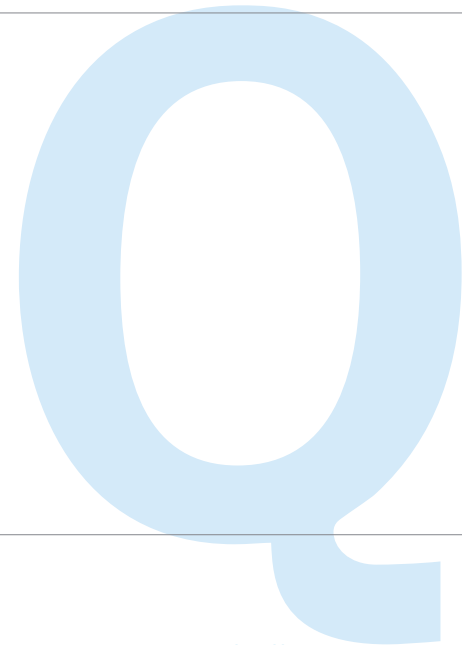
For further information of the implications of our CR agenda see page 6

For further information on how we are meeting our objectives see pages 12 to 14



For more information, and regular updates visit: [www.baesystems.com](http://www.baesystems.com)

# Key issues for our stakeholders



These are some of the questions on issues relating to corporate responsibility that we have received from stakeholders during 2006:

**The UK newspaper 'The Independent' recently claimed that out of the 33 UK companies who took part in the Carbon Disclosure Project, BAE Systems was the company doing least by far to cut its CO<sub>2</sub> emissions. Why is the company not addressing the issue of climate change?**

The article in 'The Independent' referred to a study by the Carbon Disclosure Project. We provided data we have publicly available, but some of this was not included in the research. We have been in dialogue with the company involved, they have repeated their analysis to take this information into account and the new research carried out gives BAE Systems a score of 40 (up from 25) – which now places us 4th (previously 9th) out of a total of nine in the aerospace and defence category. We already have energy management plans in place and have engaged external stakeholders on what BAE Systems responsibilities are with regard to climate change. This will form the basis of the development of a policy during 2007 (see page eight).

**What is the nature of your business with Saudi Arabia?**

The programmes we provide for the Kingdom of Saudi Arabia (KSA) are delivered as part of an agreement between the governments of the UK and KSA. We are pleased to have enjoyed a long relationship with the KSA as a valued customer. We recognise the critical role that KSA has with regard to stability in the Middle East region and are pleased to support the UK Government in this regard.

**Many CR reports tackle human rights as a CR issue. Can a defence company address this issue?**

Human rights is an emerging CR issue for many companies and one from which we are not exempt as a defence company. We have been working with external and internal stakeholders for some time to properly understand the specific human right's issues which affect our business and to put in place a human right's policy which successfully addresses these.

BAE Systems respects all fundamental human rights and will be guided in the conduct of its business by the provisions of the United Nations Universal Declaration of Human Rights (UNUDHR) and the International Labour Organisation (ILO) core labour standards.

**Do you take advantage of different legislative regimes to effectively sell anywhere you want to?**

BAE Systems is committed to complying fully with all the laws governing defence export sales in every country in which we operate. We only export from our home markets i.e. UK, US, Australia, Sweden and South Africa and do not "forum shop" to transact from countries with lax export controls. We recognise and respect the right of every national government to determine the necessary criteria for defence export sales.

**What have you done to address the concerns raised by John Wall (General Secretary, CSEU) in last year's report, that you are not doing enough to increase diversity and blow away the myth that manufacturing is a man's job?**

BAE Systems is committed to equality of opportunity for all employees and to creating a workplace where everyone is treated with respect. Gender was the key focus of our diversity and inclusion efforts during 2006 and a full report on the progress we made can be found on page 12.

Our current demographics reflect our heritage and industrial sector but we do not use that as an excuse and are committed to increasing the diversity of our workforce. We recognise that diversity of views and approach delivers the challenge and breadth required to ensure a high performance culture.



## Is there any substance in the ongoing media allegations on bribery and corruption?

We are disappointed that recent media coverage is proceeding on the assumption, unsupported by any evidence, that allegations against BAE Systems are true and offences have been committed. We continue to reject these allegations.

Employees of BAE Systems are proud to work for a company which supports the government and men and women of our armed forces, who work to protect national and international security. We take our obligations under the law extremely seriously and will continue to comply with all legal requirements around the world.

### In last year's report Robert Barrington claimed that BAE Systems was a laggard in corporate transparency. What have you done to address this?

BAE Systems was instrumental in establishing the UK Defence Industry Anti-Corruption Forum in 2006. Representatives from 11 companies and two Trade Associations held an inaugural meeting of the forum in May. The creation of this forum reflects the shared determination of the key industrial partners to promote the prevention of bribery and corruption in the international defence market. All the participants in the inaugural meeting of the forum have policies in place that meet high ethical values, backed up with compliance procedures to ensure that their employees observe the laws in all the countries in which they operate. Their aspiration is that the forum will help build on those policies and practices to ensure universally high standards in the global market.

### More and more businesses are being held responsible for the complete lifecycle of their products. The defence industry should be no exception so what are you doing in this regard?

We recognise the serious nature of our products and the duty of care we have to ensure that they are safe for the user. We already have through life responsibility for many of our products and the extent of this will increase as we move to a 'through life support' model of working with our customers. This includes both product safety and environmental considerations.

A number of media articles during 2006 ridiculed us for our work on minimising the environmental impact of our products and we will continue to utilise current and emerging technologies to achieve this.

During 2006, we initiated a debate with internal and external stakeholders on what sustainability means to a defence company. A report on this is provided on page eight.

### What was BAE Systems view on the decision to cease the SFO enquiry into Saudi?

We believe a timely conclusion to the investigation was required. It is not reasonable or just that such investigations and associated allegations which are unsupported by evidence, should continue indefinitely.

### Do you pay commissions to advisors or consultants, to win export sales?

Companies operating in global markets, in any industry, need access to local advice, capabilities and guidance in order to pursue business. It is perfectly legitimate that such advisors/consultants are paid for what they do. As with all aspects of our business we audit these arrangements to ensure that no impropriety is taking place and that we are receiving value for money for their specialist knowledge and capabilities.

### The UK Health & Safety Executive claim that 6.7 million working days are lost each year due to the effects of workplace related stress. What are BAE Systems doing to address this issue for its workforce?

We are committed to protecting the health, safety and wellbeing of our employees. We are a high performing company and recognise the pressure that this can place on individuals. Our People Policy is based on the principles of good management provided by the UK Health & Safety Executive (HSE) which are intended to minimise the factors which can lead to work related stress. A commitment has been given by our CEO and Group HR Director to the trade unions that we will develop this further during 2007.

### In 2006 one of your objectives was to ensure all employees were trained on ethics. Was this because you don't think your employees are ethical?

The decision to train all UK employees on ethics followed an employee ethics awareness survey carried out in 2005 which showed a lack of knowledge amongst our employees of the specific requirements of our ethics policies and the ethics helpline. Training programmes in business principles and integrity were already mandatory for senior employees.

The training was introduced to tackle this specific awareness issue and not because we in any way believe our employees are unethical. This is a key aspect of our corporate responsibility agenda and one we take extremely seriously.

## Have we answered your questions?

These are only some of the questions we have been asked by our stakeholders during 2006. Additional questions and answers on issues including defence exports, nuclear weapons and media allegations can be found on our website.



For more information, and regular updates visit: [www.baesystems.com](http://www.baesystems.com)

# Forward thinking

Strategic direction

Our Group strategy is 'To deliver sustainable growth in shareholder value by being the premier global defence and aerospace company'. This requires us to take a position at the forefront of corporate responsibility within our industry and aspire to perform on a par with the leading companies in other sectors.

We are developing a CR agenda for the company to support delivery of our Group Strategy. This will be based on an assessment of stakeholder expectations, taking into account the CR issues particular to the defence industry and recognising that the company will progressively be judged against peer companies in other sectors. We have also commissioned 'Article 13' an independent consultancy to review trends in CR, geographical differences and other external influences that will have an impact on stakeholder expectations.

Achieving our goals requires that all our businesses implement company policies and deliver goals set in their own CR plan. A key aspect of our CR agenda will be to maintain good business practice and continual improvement across our businesses.

Our approach to the evolution of our CR agenda is discussed above.

### CR Trends

The overall trend in progressive corporate responsibility is a move from being reactive or passive to taking an increasingly proactive approach. This implies that companies, in addition to addressing their own operating issues of safety, environment, community, ethics and people, will also play a key role in driving higher standards for specific sector or regional issues. Our strategic intent requires us to implement policies and standards across our operating regions and to extend these across our supply chain and sector.

Increasingly business is also expected to demonstrate responsible product stewardship and to understand and manage the impacts of the production, operation and end of life of its products. We have commenced this debate in relation to the environmental sustainability of our products (see page eight) and will extend this further to include other broad aspects of our corporate responsibilities.

### Implications of our Group strategy on our CR Agenda

#### Sustainable growth

Process and policies to support management of reputational issues, address long term capability aspects and anticipating development of trends

#### Global

Peer group extended beyond defence & aerospace sector, common application of standards, expectation of leadership in sectors (transparency, improving standards, product stewardship)

#### High Performance

Leadership position, capability and reputational issues addressed and managed

#### Sharing & partnership

Supply chain management and cultural development to support different way of working

#### Emerging growth markets

Appreciation (and valuing) of cultural difference and addressing issues associated with different regions

### Green thinking

## Globalisation putting many unlikely sectors in the line of fire

Human rights issues around the world are now beginning to lay the groundwork for the remaining companies that industry becomes increasingly global, its exposure to such risks. This is the case for many companies which very fine business

## Thinking bigger & better

Social enterprise is for more than just small community projects, it is an important model for running big businesses and public services. Should some large companies, such as those involved with water and energy not be social enterprises? By the same token those who are

## What is sustainable growth?

## ‘ Looking ahead to 2007, the Company is committed to a more proactive approach to CR through the alignment of the CR agenda with the company strategy .’

### External Issues

There are some issues which will impact all businesses to some degree regardless of their sector. These include global warming and differences in attitude and approach of each generation (to the world in general and specifically the workplace). We need to understand the potential impact of such issues on our environment and business and develop appropriate responses.

Terrorism has changed the nature of warfare and how people regard security and conflict. Our industry must respond to the changing requirements in technology and equipment both for warfare and the ever increasing role of delivering humanitarian aid and peacekeeping.

### Geographical Influences

CR primarily relates to the responsibilities companies have with regard to the workplace, communities and environment with the emphasis on particular aspects being influenced by local or national concerns and cultural differences. Our global aspirations require us to understand and value these differences and consider how to optimise our operations to best effect.

### Next Steps

We will continue to debate these issues and the implications of our Group Strategy, against a rolling plan, with our Executive Committee, CR Committee and Board of Directors.

We will continue to engage with stakeholders on the general direction and performance of our CR agenda.

### Corporate Responsibility Committee

**Peter Weinberg**  
Corporate Responsibility  
Committee Chairman



#### Members:

Peter Weinberg (Chairman)    Phil Carroll  
Professor Sue Birley            Sir Nigel Rudd

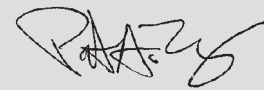
#### Responsibilities:

- Assist the Board in overseeing the development of strategy and policy on social, environmental and ethical issues.
- Monitor and review the Company's performance in managing environmental, social and reputation risks. Specifically, the Committee shall review whether there are appropriate policies, systems and metrics in place to manage, monitor and review social, environmental and ethical risks to the Company. These shall include, but shall not necessarily be restricted to, health and safety, workplace policies, responsible supply chain management, environmental impact, business ethics and compliance with law and regulation.
- Review the Corporate Responsibility report prior to approval by the Board of Directors.
- Oversee and support key stakeholder engagement on social, environmental and ethical issues.
- The Committee Chairman shall report to the Board on the proceedings of the Committee on a regular basis.

#### Message from Peter Weinberg on behalf of the CR Committee.

The primary focus of the CR Committee during 2006 was on understanding, reviewing and monitoring the policies and processes in place to manage social, environmental and ethical issues. Key areas reviewed included health and safety, appointment of advisors and business ethics. Based on our reviews to date we are satisfied that the Company has established a good basis for its CR activity and recognises that this is an essential part of good business management.

Looking ahead to 2007, the Company is committed to a more proactive approach to CR through the alignment of the CR agenda with the company strategy. The CR Committee, in conjunction with the Executive Committee, will agree the development and direction of the CR agenda, through the setting of policies and goals to achieve its delivery. We consider this to be an important aspect to ensuring the sustainability of future business activity and anticipate further progress during 2007.



**Peter Weinberg**  
Corporate Responsibility Committee  
Chairman

# Debating the future

## Introduction

Our company is a global business, with operations and customers in many countries. Stakeholders expect us to understand and respond to global challenges such as climate change, human rights and sustainable development. In 2005, the assurers of our CR report recommended that we publish our position on these issues.

We are exploring these subjects in more detail to find out what stakeholders expect from us and the implications for our business.

In November 2006 we held a discussion on the significance of environmental sustainability for BAE Systems. We invited four opinion leaders with relevant expertise to meet with senior managers from the CR, legal, engineering and media departments at BAE Systems and representatives from the UK Ministry of Defence.

Participants debated two subjects relating to environmental sustainability:

- Product stewardship and the environmental impact of our products; and
- Climate change.

**Stakeholder engagement informs our corporate responsibility strategy and approach to managing and reporting on CR issues.**

‘Despite the snigger factor of ‘green bullets’, there is no reason why BAE Systems should be treated differently from any other large manufacturing company whose products have an environmental impact.’

Rob Lake, Socially Responsible Investment Analyst

## Product stewardship

### Is product stewardship a relevant issue for BAE Systems?

Recent news stories have mocked product stewardship initiatives such as lead-free bullets. It has been suggested that this is an attempt to ‘greenwash’ the image of defence companies and distract attention from their core business. However, participants agreed that product stewardship is a relevant issue for BAE Systems for environmental and business reasons:

- Ordnance left over from wars or military training can have a significant impact on the environment and potentially on the health of local communities. Disposal of old ships and aircraft can damage the environment if hazardous substances aren’t identified and disposed of safely.
- Environmental issues are now higher up the agenda for governments and major customers, such as the UK Ministry of Defence, are starting to take them seriously.
- Investors increasingly expect all companies to be addressing environmental issues. They consider environmental management as one indicator of overall management quality.

It was accepted that many strong critics of the defence industry will inevitably dismiss product stewardship as a distraction, but most stakeholders expect BAE Systems to be good stewards. This is because they see the company having the same environmental responsibilities as any other major manufacturer.

### Whose responsibility is it?

There was debate on the respective responsibilities of the UK Ministry of Defence (UK MoD) and BAE Systems on who should drive improvements in product environmental performance.

Opinion was that there is a shared responsibility between the customer and supplier for product stewardship and both parties should do more to tackle the issue.

It was agreed that changes to BAE Systems business model could have a beneficial impact. Over the next ten years BAE Systems



**Wars end and you have to live with the peace afterwards. The inefficiency of war and its environmental impact on the world is a real issue for BAE Systems.**

John Mumford, Imperial College

expects to shift from being primarily an equipment supplier to becoming a through life service provider (including the disposal of end-of-life products). This will encourage the company to improve the environmental performance of products, and to use materials that can be easily recycled when the products are scrapped.



**Why aren’t you as passionate about the environment as you are about combating bribery and corruption? You shouldn’t be reactive. Being a leader on environmental performance and shaping new regulations will save the company money in the long term.**

Aled Jones,  
Cambridge Programme for Industry

### Way forward

Participants want to see BAE Systems shaping the debate on product stewardship and influencing UK MoD requirements and regulations. They expect product stewardship to become more important to the UK MoD and other customers and believe that BAE Systems could gain competitive advantage by being an early mover. This could also reduce costs and benefit the company’s reputation.

It was suggested that BAE Systems needs to devote as much energy to these issues as it has to its ethics and anti-corruption programmes.



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# Our strategic direction (continued)



The UK Ministry of Defence could drive progress by setting environmental performance requirements for its suppliers. This would provide a clear steer to the company and provide an impetus to invest in environmental technology.

It was suggested that the partnership approach set out in the Defence Industrial Strategy provides a model for the UK MoD and company to collaborate to benefit the environment.

A first step could be a joint analysis of the life-cycle costs of a product, including disposal. This would demonstrate whether factoring in the cost of disposal could be a cost saving measure.



**We're looking at initiatives to help reduce the environmental impact of ship disposal. We are designing out hazardous materials at the start so there are fewer issues to deal with at the end of a vessel's life.**

[Henrietta Anstey, BAE Systems](#)



**Our employees look for leadership from us on key issues. They want to know where the company is coming from and what it stands for. They see nothing on climate change and it's a real opportunity for us to do something.**

[Simon Howison, BAE Systems](#)

## Climate change

### Is climate change important to BAE Systems?

It was agreed that climate change is now a serious issue for all companies as well as individuals and governments. Participants expect these trends to continue to increase as more is learnt about the science of climate change.

All participants expected BAE Systems to take climate change seriously and to develop an effective strategy to tackle it. This should include plans for reducing its greenhouse gas emissions and preparing for the risks and opportunities presented by climate change.

It was noted that this could improve the company's relationships with three significant stakeholder groups:

# ‘BAE Systems is in a carbon unknown state. It’s managing its energy but hasn’t yet recognised what impact climate change will have on its business.’

Peter Martin, CarbonSense

- Some investors want to know that companies in their investment portfolio have a strategy for responding to the risks and opportunities of climate change.
- The UK government has placed climate change high on its agenda following the Stern Review. There have been parliamentary questions on CO<sub>2</sub> emissions from military training flights and discussions on the potential impact of climate change on national security. The UK Ministry of Defence aims for its office estate to achieve carbon neutrality by 2012 and will expect suppliers to help them reduce their carbon footprint.
- Employees would appreciate BAE Systems articulating a clear policy on climate change. It was felt that employees would respond positively to the company adopting a leadership stance on this issue and this could benefit morale and productivity.

## What are the risks and opportunities?

Participants mentioned several potential risks and opportunities for BAE Systems. These included changes to products, which will need to function in higher temperatures and more extreme weather will increase demand for rescue equipment, as demonstrated by Hurricane Katrina.

## Views on BAE Systems current approach

Disappointment was expressed that BAE Systems does not yet have a climate change strategy. Although the company has processes for managing its energy use, they felt it had not yet thought through the implications of climate change for its business or identified where risks and opportunities might arise.

## What should BAE Systems do next?

Four main actions were called for:

- Identify the risks and opportunities of climate change for BAE Systems.
- Integrate this analysis into the company’s strategic planning and decision-making.
- Involve people from across the company – don’t try to manage this from the CR department.
- Help set the agenda on climate change through interactions with governments.

## Next steps

The initial stakeholder engagement session has taken us forward by clearly indicating that both internal and external views are that irrespective of our sector we need to address issues of environmental sustainability and climate change.

In response to this we will continue to evolve our position and develop a pragmatic response appropriate to our products and operations.



**The Ministry of Defence aims for its office estate to be carbon neutral by 2012 and will expect suppliers to help them reduce their carbon footprint.**

[John Cole, UK Ministry of Defence](#)

## Participants

### Kathryn Charnaud

Environment Department,  
UK Ministry of Defence

### John Cole

Defence Directorate of Safety and  
Claims, UK Ministry of Defence

### Aled Jones

Development Director, Cambridge  
Programme for Industry

### Rob Lake

Socially Responsible Investment Analyst

### Peter Martin

Director, CarbonSense

### John Mumford

Professor of Natural Resource  
Management, Imperial College London

### Deborah Allen

Corporate Responsibility Director,  
BAE Systems

### James Baker

Director of Technology & Engineering  
Services, BAE Systems

### Mike Elston

Head of Legal Services,  
BAE Systems – Land Systems

### Lisa Hillary Tee

Media Relations Manager,  
BAE Systems

### Simon Howison

Group Engineering Director,  
BAE Systems – Air Systems

### Leigh Munro

Corporate Responsibility Manager,  
BAE Systems

### Henrietta Anstey

Environment Manager,  
BAE Systems – CS&S Naval



# Progress and performance

## Workplace

3 For details of our Objectives for 2007 see page 3.

The Group employs 79,000 people (in its wholly owned businesses) across five continents, the majority being based in the UK and the US, with a significant presence in Saudi Arabia, Australia, South Africa and Sweden.

To deliver the products and services our customers require we need to attract and retain a highly talented workforce. We do this with a focus on a high performance culture which, in addition to setting out goals and objectives, also defines the behaviours we expect of our employees.

### 2006 Objectives

- In 2006 two workplace related objectives were set as part of the leadership objectives for the Group's senior executives.
- Reflect gender diversity on leading university courses in our choice of graduate trainees through a focused recruitment plan.
  - Resolve 75% of employee grievances in the UK at local level (i.e. drive solutions to employee issues through effective local management).

### Progress

#### Diversity

We met our targets to recruit at least an equal proportion of female graduates to those seeking a career in engineering. Over the year, 12% of our UK and 20% of our US engineering graduate recruits were women.

Our Group HR Director, Alastair Imrie, was nominated as our senior Gender Champion with a remit to raise awareness of potential barriers to the career progress of women in the Group and to identify ways to address those potential barriers.

Recognising that the Group's senior leadership plays a significant role in influencing behaviours, a number of our senior female

managers represented the company at events in support of groups such as the International Women of Excellence and the International Women's Forum. Junior female employees also attended these events as participants. An outcome of this representation was the initiative to establish a women's network at our Submarines site at Barrow in the UK as a pilot to assess the potential to develop further network groups elsewhere across the business.

We participated in a workshop with senior female managers from the UK Ministry of Defence to discuss barriers to gender progression within each of the respective organisations and to explore mutual areas to address.

#### Respect at Work

97% of employee grievances in the UK were resolved at a local level during 2006. Only one complaint required a corporate level investigation under the Group's Respect at Work policy. This indicated improved management and resolution of issues at a local level.

In the UK, we have continued to work closely with the DTI and AMICUS on the Dignity At Work partnership. This year the partnership launched research into the impact of bullying in the workplace and hosted several high profile events to raise awareness of this important issue.

#### Training and Development

In the UK employees completed 38,000 e-learning courses (equating to 24,000 hours of online training time). Employees and their families have access to 1,500 courses, many of which are run in partnership with colleges and universities.

In the US we have invested in employee development and recent executive appointments from within our leadership

ranks demonstrate career growth opportunities. Two new CEO sponsored leadership programmes were introduced in 2006 and delivered to more than 600 executives in the US and UK.

#### Employee Recognition

We reward employee excellence and innovation through the Chairman's Awards Scheme. Over 3,000 nominations were received for 2006, recognising over 17,000 employees from around the world. From those, six Gold, 54 Silver and over 100 Bronze awards were awarded across the three categories of Innovation, Transferring Best Practice, and Enhancing Customer Performance.

#### Employee engagement

In 2006, more than 45,000 employees (over 64% of the workforce) took part in our bi-annual global Employee Opinion Survey (EOS). Overall the results were encouraging with clear improvement reported against 2004 performance.

The greatest improvements were in career development and rewards, trust in leadership and engagement. The most negative score related to our employees' perceptions as to how poor performers are managed. While this reflects the high standards our employees expect of the company, it is an issue of concern which the Executive Committee has committed to improve in 2007. See table below.

### Employee opinion survey (EOS)

Positive Increases Question	% Fav 2006	Change from 2004	Negative Increases Question	% Fav 2006	Change from 2004
I have access to the training I need to be productive on my current position	68	10	Poor individual performance issues are addressed effectively where I work	33	-3
I have confidence in the job being done by the senior management of BAE Systems	52	9	I am supported and encouraged to make my own decisions	74	-3
I would recommend BAE Systems to others as a good place to work	68	6	In my team we get regular feedback on how satisfied customers are with the work we perform	54	-2
I understand how my job contributes to my Business Unit/Line of business in achieving its business plan	84	6	My immediate manager/team leader lets me know how I'm doing on an ongoing basis	56	-2

# ‘We will not tolerate unethical behaviour or attempts to improperly influence the decisions of customers or suppliers.’

## Ethics

3 For details of our Objectives for 2007 see page 3.

**We are committed to meeting the highest ethical standards in our dealings with others. We will not tolerate unethical behaviour or attempts to improperly influence the decisions of customers or suppliers. Unethical behaviour is wrong, could lead to loss of business, seriously damage our reputation and leave the Group and its employees open to criminal sanction.**

### 2006 Objectives

In 2006 two objectives specifically relating to ethics were set within the leadership objectives.

- Meet the standards defined in our internal assurance statement (for ethical issues, the minimum acceptable score within our assurance process is confirmation of compliance with all applicable laws and standards).
- Develop, pilot and roll out ethics training to all employees in the UK and Australia.

### Progress

#### Meeting our standards

The Group has training and awareness programmes to ensure employees understand our policies and the standards expected of them.

We provide training on our anti-bribery programme to managers from commercial, procurement, finance, customer support and other functions as well as marketing staff and other senior managers. On completing the training, employees are required to sign a statement confirming they will comply with our policies and will report any issues of concern. This training is mandatory for all senior employees and for those employees involved in dealings with marketing advisers. All BAE Systems' marketing advisers are subject to rigorous due diligence under our compliance programme, are made aware of

our anti-bribery policy and are expected to maintain our ethical standards.

#### Awareness and Training

A survey of UK employees undertaken in 2005 showed that although our employees regard the Company as ethical, awareness of our ethical standards and helpline was low. In 2006 we introduced new online training for all UK employees covering: 'What is Business Ethics and Why is it Important to Me?', 'Why Following the Law is not Enough' and 'Examples of Ethics in the Workplace'.

Employees must complete a test at the end of the course to measure understanding of the issues raised during the training. A DVD and classroom training package was used for employees who did not have ready access to a computer. Both training packages were introduced and endorsed by our Chief Executive, Mike Turner.

By the end of 2006 80% of UK employees had successfully completed the training. Plans are in place to ensure the remaining 20% complete the training early in 2007. We missed our target to train all employees in Australia during 2006 but intend to roll out the training to all employees in Australia, South Africa, Saudi Arabia and Sweden during 2007.

In the US, all employees completed refresher training on our workplace harassment and ethics policies, and ethical decision making. All employees receive annual training on ethics related topics. This year all employees viewed a new ethics video called 'Playing With Fire: Abuse and Intimidation in the Workplace'.

We held our annual conference for BAE Systems ethics officers in Baltimore, US. More than 50 participants from the US, the UK and Sweden were joined by speakers

from the US Department of Defense and the Ethics Resource Center. Experts led training sessions on ethics investigations and regulations on harassment and violence in the workplace.

During 2006 we also held ethics training for the Board and Executive Committee, debating and agreeing the role of leadership in ensuring high ethical standards throughout the Group.

#### Monitoring and compliance

In 2006, 62 enquiries were made to our UK ethics helpline and worldwide e-mail address, compared with 31 in 2005. These covered a variety of topics, but primarily concerned workplace issues and acceptable IT use policy. In the US, there were 348 formal enquiries (including 186 requiring formal investigation) to ethics officers via our helpline, post, email or visits to the ethics office.

50 employees were dismissed for reasons relating to unethical behaviour during 2006. Reasons for dismissal included misuse of company IT, fraud, inaccurate labour charging and threatening behaviour.

#### Working with others

In early 2006 BAE Systems and other UK defence companies established the UK Defence Industry Anti-corruption Forum, to share good practice on ethics and anti-corruption programmes. Members of the Forum met twice in 2006 and heard from a range of speakers including the Institute of Business Ethics, ICC (UK), Transparency International (UK) and law firms, Linklaters and Bryan Cave LLP.

In the US we are a signatory to the Defense Industrial Initiative on Ethics and Business Conduct. We are also a sponsoring partner of the Ethics and Compliance Officers Association.

## Our ethical principles are:

**Accountability:** We are personally answerable for our conduct and actions

**Honesty:** There is no substitute for the truth

**Integrity:** We say what we do, we do what we say

**Openness:** When questions are asked, we will be frank and straightforward in our answers

**Respect:** We value and treat each individual with dignity and thoughtfulness

## Safety, health and environment

3 For details of our Objectives for 2007 see page 3.

The health and safety of our employees, contractors and engagement with the communities around our facilities is of primary importance to BAE Systems.

We recognise the risks associated with the variety of operations we conduct and aim to minimise these as far as possible. All sites are required to comply with our Safety, Health and Environment policy and to demonstrate continual improvement in performance through the setting of targets. Performance is reviewed through our business assurance processes and overseen by the Executive Committee and the CR Committee on behalf of the board of directors.

Our environment policy and framework is focused on preventing or controlling environmental impacts and minimising waste (or consumption when related to energy and water). All our major manufacturing sites are certified to the international environmental management standard ISO 14001.

### 2006 Objectives

In 2006 two objectives specifically relating to ethics were set within the leadership objectives.

- Meet our safety, health and environment targets (performance improvement criteria appropriate to risk established at global business unit level.
- Exceed the safety performance commitments made to the UK Health and Safety Executive.

### Progress

Targets were set against individual businesses and all businesses included Safety, Health and Environment in their quarterly management reviews. The overall

performance on safety reflects the good performance against these targets. Compared with 2005 both the overall number of accidents and the number of serious accidents decreased in 2006. The majority of our business continue to demonstrate improvements (i.e. reductions) in the days lost to work related injuries indicating both a reduction in the number of accidents and length of time for rehabilitation back into the workplace. The increase indicated in the table on page 30 reflects the inclusion of a full year of data for our US ship repair business and does not indicate a significant deterioration. The commitments made as part of the UK Government's 'Revitalising Health & Safety' initiative have been exceeded – that is – we have already met targets for performance by 2010.

### Partnership with the UK HSE

We continued our partnership project with the UK Health and Safety Executive (HSE) and other large UK manufacturers. The project, named Large Organisation Partnership Pilot (LOPP), aims to raise safety standards in UK manufacturing sites.

In 2006 a joint team of BAE Systems managers, trade union safety representatives and the HSE developed key performance indicators (KPIs) in six areas:

- Work at height
- Control of contractors
- Hand-arm vibration
- Work in confined spaces
- Slips and trips
- Manual handling

These KPIs are used by our business units to monitor and improve performance through an audit programme. Eight of our UK sites were audited against the relevant topic standard during 2006. Only one audit failed. Improvement actions were put in place and

a follow up audit confirmed that corrective actions had been implemented.

We are communicating the output of these audits to all our UK businesses through news bulletins, office and workshop talks and a training DVD. Employees can also access the information on our LOPP web site. We will continue to use the audit programme as part of our drive for high performance across all areas of safety, health and environment.

### Environment

The environment data shown on page 26 reflects the numerous changes to our business and activity over the last four years. We monitor trends at an individual site level and continue to see reductions in both water and energy consumption.

The overall data now includes the former United Defense businesses and these account for the increases in consumption. Whilst the use of natural resources is driven by the growth of our business we remain committed to delivering ongoing operational efficiencies and improvements in this area.

### Waste Electrical and Electronic Equipment (WEEE) Directive

The WEEE Directive became effective in January 2007 requiring producers of certain electronic equipment to account for end of life disposal. During 2006 we conducted reviews to assess the impact of this Directive and put in place measures to monitor and manage the issue going forward.

‘In the 18 months to September 2006, our global employee fundraising scheme, Charity Challenge, raised £8 million.’

## Education and community

**Education, specifically in the fields of science and engineering, is extremely important to the future sustainability of our business.**

**The number of students enrolling in engineering and technology courses has fallen considerably in recent years. We are concerned that in the future there will be too few candidates with the skills our business, and the engineering sector in general, needs.**

### Education

In Australia, Saudi Arabia, the UK and the US we run an education programme that encourages young people at all stages of their education to take an interest in science and technology.

### UK

Over 350 employees (known as ambassadors) visited schools to help with engineering projects and to give careers advice.

Our schools road show is designed to encourage children to think about a career in engineering before making subject choices at 14. The 2006 road show, visited 100 schools, involving 10,000 children aged 9-13 in performances and workshops. In 2006 our education programme was awarded a Business in the Community ‘Big Tick’ Award and was a finalist in the Opportunity Now Awards.

We participated in Enterprise Week 2006 delivering a schools road show performance at an Enterprise in Education conference. We have strategic partnerships with 20 colleges and universities to support research and improve graduate recruitment.

BAE Systems has made a commitment to be one of the ‘corporate champions’ behind the British Council’s UK India Education & Research Initiative. As part of our commitment we will be supporting links between schools in Brough in the UK and Bangalore in India, an exchange of best practice in vocational

training and an innovative research project on Unmanned Aircraft Vehicles linking Leicester University with the Indian Institute of Science at Bangalore.

### US

We sponsor a number of programmes to support science and technology across the US. Our scholarships to colleges and universities have enabled hundreds of students to take technical courses. In 2006 this support included: providing project challenges and mentors to Penn State’s Learning Factory; sponsorship of Science and Technology Way – an open house showcase held at the University of Maryland; and the sponsorship of the annual Rube Goldberg Machine Contest held at Purdue University.

### Saudi Arabia

BAE Systems’ long association with academia from the Kingdom of Saudi Arabia has continued with the funding of research carried out by Saudi lecturers in the UK.

Following completion of the four-year Saudi government campaign to establish national vocational skill standards, backed by BAE Systems, the Group sponsored a conference on the next round of challenges facing those in the vocational training establishment in meeting the needs of the Saudi labour market.

The Saudi-British sports co-operation programme, which began in 1987, had its most active year to date in 2006. This BAE Systems-managed project is geared to the raising of standards and the introduction of new sports, and takes as a main aim the education of administrators, medical practitioners, coaches and others who will stimulate the development of the sector.

### Australia

In Australia BAE Systems supports a wide range of school and university programmes.

The Group works with these institutions, offering sponsorship and mentoring programmes, with the aim of inspiring young people to get involved in engineering. These projects include sponsorship of South Australia’s Engineering Week and Super Science Sunday; involvement with the Doxa Youth Foundation mentoring programme and support for the Young Achievement Australia Business Skills Programme.

### Community

#### Employee Involvement

In the 18 months to September 2006, our global employee fundraising scheme, Charity Challenge, raised £8m. This was donated primarily to the Stroke Association in the UK, the National Heart Foundation in Australia and the American Cancer Society. Over the same period, employees volunteered 10,500 days of their own time. Our partner charities for the next 18 month campaign will be the Macmillan Cancer Support in the UK, the Australian Cancer Council and the Alzheimer’s Association in the US.

#### Company Giving

In 2006 our total global community investment was £8,223,160. This figure includes cash and in-kind donations as well as our direct support for education.

We are a member of the London Benchmarking Group (LBG) and use their agreed methodology to evaluate our annual community contributions.

### Community investment – what we contribute to (%)



# Driving CR across the business

## Electronics Intelligence & Support

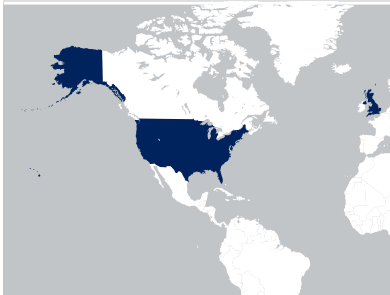
This report addresses our Corporate Responsibility issues and priorities at group level.

We believe it is equally important to demonstrate how our business is organised and the specific CR issues faced at business group level. The following pages give an overview of the key highlights and initiatives across our six global business groups.

### Principal operations

Provides a variety of military communications, electronic identification, navigation and guidance systems, network-centric warfare solutions and a broad range of support solutions, including major ship repair activities for the US Navy.

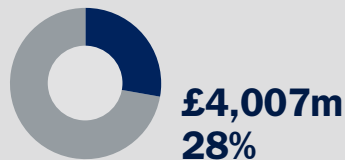
### Main operating locations



### Major markets

US, Global

### Share of 2006 Group Sales



### Number of employees

31,700

### Electronics & Integrated Solutions

#### Highlights for 2006:

- Introduced closed loop cooling systems at our Fort Wayne, Indiana; Johnson City, New York; and Greenlawn, New Jersey sites. This will reduce annual water consumption by 100 million gallons and reduce the risk of releasing ozone depleting refrigerants (CFCs) into the environment.
- Implemented a full environmental, safety, and health (ESH) management system at our Ontario, California site.
- Retained Occupational Safety and Health Administration Star status at our Johnson City site. ISO 14001 and the Occupational Health and Safety Assessment Series registration maintained at selected sites and our Cheshire, UK site became ISO 14001 registered.
- Implemented an on-line Material Safety Data Sheet (MSDS) system at our Ft. Wayne facility to enable employees to access MSDS and print chemical container labels at the point of use.
- Raised \$68,000 for the Juvenile Diabetes Research Foundation.

#### Building cleaner, more efficient buses

Electronics & Integrated Solutions is working with the US Federal Transit Administration (FTA) to demonstrate fuel-cell technology for city buses. The fuel cell will use hydrogen to generate power cleanly and quietly, with water and heat as the only by-products.

The fuel cell will be integrated into a hybrid diesel-electric bus made by DaimlerChrysler. It will power the air conditioning, air compressors, power steering and other systems that ordinarily run off the engine. Switching the power source to a fuel cell allows the engine to be shut off at bus stops and at traffic lights, making the bus quieter, cleaner and more efficient compared to a conventional diesel bus.

The FTA has awarded \$5.35 million for the project to be distributed over four years by WestStart CALSTART, a non-profit organisation that promotes clean, energy efficient transportation technologies.

BAE Systems is a founding member of CALSTART and is represented on its board of directors.

John Boesel, president and CEO of CALSTART said, "We are pleased to join with BAE Systems – a company recognised for its pioneering work in hybrid drive systems – on this important project."

### Platform Solutions

#### Highlights for 2006

- Won the BBC Radio Kent, Healthy Large Employer Award for our monthly health clinics and weight management programme.
- Ran an employee awareness campaign to reduce winter accidents.
- Won the Royal Society for the Prevention of Accidents Gold award for continual health and safety improvements for the fifth year running.
- Won the International Safety Award from the British Safety Council for the sixth year in a row.
- Our Rochester site received Institute of Engineering and Technology approval for its apprentice training programme.
- Helped send 80 students to the Farnborough Air Show, International Youth Day for a day of engineering activities.
- Most improved site at Charity Challenge Awards.

#### Working with local schools

Platform Solutions is helping to prepare young people for life after school. We are partnering with the Medway Education Business Partnership (MEBP), a charity working to improve the links between schools and businesses around Medway in Kent.

MEBP run their campaign from an office at our Rochester site and Platform Solutions HR Director, Mark Bowers, sits on the charity's board.

Our employees donate money and time to help MEBP. This year, 11 employees mentored students from schools around Medway (a further 15 are now being trained as mentors).

Through MEBP, we support Young Enterprise, an initiative which aims to teach children business skills. In 2006, four employees visited schools for two hours each week to help children run small enterprises they have set up through the scheme.

We also host Work Related Learning Days to get young people interested in engineering. Pupils from local schools come to the Rochester site for the day and are set engineering challenges.

In total Platform Solutions employees donated 500 hours in support of MEBP.

### Customer Solutions

#### Highlights for 2006:

- Our San Diego Ship Repair site was awarded 'Star' status and accepted into the Occupational Safety and Health Administration's Voluntary Protection Programme – one of only two private shipyards in the country in this programme.
- Our Norfolk Ship Repair site earned the Sustained Distinguished Environmental Performance Award from The Elizabeth River Project, a Portsmouth, VA-based environmental organisation dedicated to urban river restoration.
- Our San Diego Ship Repair and Hawaii Shipyards sites participated in the Bikes for Tykes programme, donating their time and effort to assemble bikes for needy children as part of the Marine Corps Toys for Tots drive.

- BAE Systems was recognised by the National Society of Black Engineers (NSBE) Alumni Extension DC Chapter for our corporate sponsorship. The award was given at their annual Scholarship and Chapter Awards Program held at Catholic University in April.

#### Innovative new toxics treatment process

We have developed a process to remove Tributyltin (TBT), a toxic pesticide, from wastewater at our Norfolk Ship Repair site in Hampton Roads, Virginia. Coatings containing TBT are applied to vessels to stop barnacles and other marine organisms growing on the hull. It is also used to make rubber sonar domes for military ships.

Until now, wastewater contaminated with TBT was transported to a disposal facility at a cost of about \$1 per gallon. During a recent cruise ship project, we disposed of more than 1.25 million gallons of wastewater in just ten days.

To help offset these financial and environmental costs we developed our own onsite treatment process which removes TBT to extremely low concentrations. On-site treatment of the TBT-contaminated wastewater costs about 10% of off-site disposal.

We believe we are the only industrial facility in the US that can remove TBT to such low levels. The new process saved us around \$4.5 million in 2005-2006.



Left: Electronics and Integrated Systems is working on a 4-year trial to demonstrate fuel cell technology for city buses.

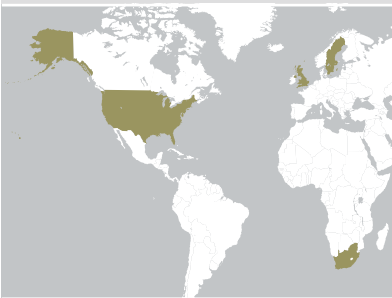
Right: Platform Solutions is helping to prepare young people for life after school.

## Land and Armaments

### Principal operations

Provides design, development, production and through-life support and upgrade of armoured combat vehicles, naval guns, missile launchers, artillery systems and intelligent munitions.

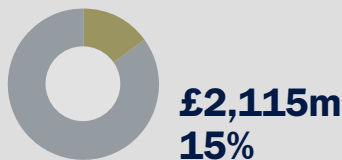
### Main operating locations



### Major markets

US, UK, Sweden, South Africa

### Share of 2006 Group Sales



### Number of employees

**11,600**

### Land Systems

#### Highlights for 2006

- Land Systems apprentices designed an Arm Rehabilitation Apparatus which stops muscle deterioration in people who are suffering from paralysis caused by strokes.
- We piloted flame resistant protective clothing designed by a team at the Land Systems Munitions business.
- We assigned a senior executive to each site to champion safety, health and environment (SHE) and monitor improvements.
- We appointed a Head of SHE to coordinate activities in this area across Land Systems.
- We launched the Start Safe Keep Safe campaign which raised awareness of health and safety using magazine articles, posters, tool box talks and road shows.
- We implemented a new trolley system to improve the safety of moving hulls at our South African business.
- We conducted a study to identify energy saving opportunities across our sites
- We developed a policy on drug and alcohol abuse.

#### Cutting costs and carbon emissions

It takes a lot of energy to heat and power Land Systems. Our buildings are huge (one in Newcastle is half a mile long) and there are a lot of them (over 1,000 at our Glascoed site). This costs a great deal of money and also contributes to climate change.

Land Systems developed a 'Wasteline' campaign over the 2005 Christmas holiday period to slim down energy bills and carbon dioxide emissions. Using workshops and posters to raise awareness of how everyone can contribute by taking even small actions, the campaign was a great success and saved £6,276 during the Christmas period across Land Systems sites.

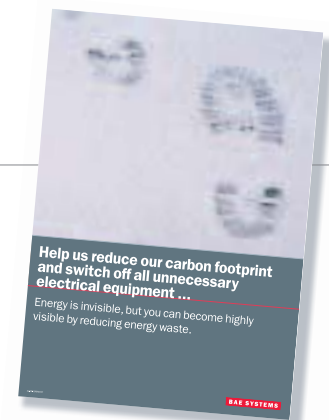
Building on this great campaign, Land Systems transferred their best practice more widely across BAE Systems in the UK. By obtaining the buy in from the BAE Systems Operations Council a small amount of funding was provided to produce new posters for the 2006 Christmas campaign. The underlying theme of the new poster campaign was that these savings should be made throughout the year and not just for Christmas, so hopefully the campaign will live on in 2007.

The 2006 Christmas 'Wasteline' campaign across BAE Systems was adopted across many parts of BAE Systems and was a great success. Using the 2004 data from Land Systems sites as a baseline, £130,000 was saved during the Christmas period, which equates to 571 Tonnes of CO<sub>2</sub>.

### Land and Armaments

#### Highlights for 2006:

- Three new manufacturing sites certified to the international environmental management standard ISO 14001.
- Set up an advisory board to ensure compliance with the Toxic Substances Control Act.
- Implemented an internal environment, health and safety (EHS) audit programme.
- Minneapolis site won the Minnesota Safety Council's Award of Honor for its health and safety performance, for the ninth consecutive year.



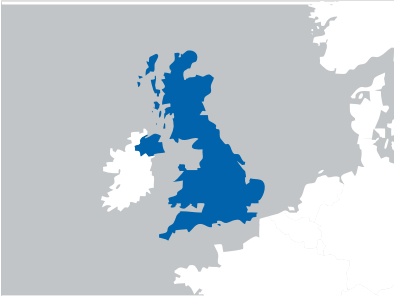
Right: Land Systems ran a 'Wasteline' campaign over the 2006 Christmas holiday period to slim down energy bills and cut carbon dioxide emissions.

# Programmes

## Principal operations

Comprises the Group's air systems, naval ships and submarines activities, with the UK MoD its principal customer.

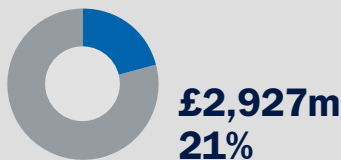
## Main operating locations



## Major markets

UK

## Share of 2006 Group Sales



## Number of employees

**17,900**

## Air Systems

### Highlights for 2006

- Agreed to contribute £10,000 over the next two years to a local authority initiative designed to make Fylde the most energy efficient borough in the UK.
- Reduced the energy needed to heat and cool our F-35 Lightning II (formerly known as the Joint Strike Fighter) facility, saving us £1,000 to £2,000 per week.
- Met regularly with local residents and other interested parties to update them on plans to develop our Samlesbury site, and address their concerns.
- Was title sponsor of a regional technology tournament for secondary schools throughout Lancashire and Cumbria, involving more than 1,000 students and technology teachers from 100 schools.
- Sponsored a local initiative to encourage pupils and their parents/guardians to walk to school every Wednesday.
- Held four 'Green Weekends' to conserve energy. Our Brough site closed from Thursday night to Monday morning, so employees enjoyed an extra day off work. Eight 'Green Weekends' are planned for 2007.
- Was title sponsor for the Lancashire emergency services annual 'Pride of Lancashire' bravery awards.
- Launched the Lean Learning Academy, a three week efficiency and leadership training programme.

### Lean Learning Academies

We launched a new training programme to teach our employees how to 'think lean'. 'Lean' is a process designed to increase the efficiency of all the work done at Air Systems – from engineering to procurement.

Forty one Air Systems employees attended Lean Learning Academies to find out how to identify and eliminate waste. The three week course teaches the principles 'Plan, Do, Act, Check' to make sure managers deliver the

actions they promise to their team. Other topics on the course include 'current and future state mapping' (assessing where you are on a project and where you would like to be) and policy deployment (making sure all levels of the organisation are geared towards meeting site targets).

Above all the 'lean' approach is about enabling our leaders to have tight control over their daily routines and the routines of their teams. This means that different parts of the business can work to the same timetable.

Another six Lean Academy Courses are planned for 2007.

## Naval Ships

### Highlights for 2006

- Developed an Energy Policy to measure and reduce energy consumption.
- Held Learning at Work Days at our Filton and Govan sites where employees were given health advice, learned new skills and were encouraged to take up new hobbies.
- Launched an Everyday Skills programme which offers courses on basic IT, communication, literacy and numeracy.
- Introduced a NVQ Level 3 Certificate training course in First Line Management.
- Introduced flexible working arrangements for non-production workers, which include a childcare voucher scheme.
- Recruited 70 new apprentices (taking our apprentice total to 250).
- Reduced accidents by 52% over the last two years.
- Accredited to Investors in People, the training and human resources standard.
- Raised around £108,000 for charity.

### Improving safety at our sites

Naval Ships is leading Group efforts to reduce risks from working in confined spaces and from hand-arm vibration syndrome (HAVS). This work is part of BAE Systems' partnership with the UK Health and Safety Executive (HSE).



Left: Air Systems launched a new training programme to teach employees how to 'think lean'.

## Programmes (continued)

### Confined spaces

In 2006, we carried out a two day inspection to assess standards for working in confined spaces at our Govan site. A team of in-house inspectors found that good training plans and rescue arrangements were in place, but identified a need for clearer guidance about what constitutes a confined space.

A follow up audit identified all confined spaces across Naval Ships. A central team was then set up to co-ordinate improvements and make sure that controls such as ventilation, lighting, signage and test certificates are in place at all sites.

The standards developed at Naval Ships will apply to all BAE Systems' employees as well as to the contractors and suppliers working for us.

### Protecting employees from vibration

Engineering equipment can cause hand-arm vibration syndrome (HAVS) which leads to a loss of sensitivity of fingertips.

Naval Ships has developed a set of key performance indicators (KPIs) for BAE Systems and guidance on how to achieve these standards.

Employees at our sites undergo regular health screenings to identify early symptoms of HAVS before the condition can become serious. Individuals diagnosed with HAVS are restricted from doing certain types of work. Our Occupational Health Department and the employee's supervisor work with the individual to agree how to limit their exposure to vibration.

Naval Ships have introduced a traffic light system to control exposure to vibration from tools. A red label means that the piece of equipment can only be used for a specified time period. Green signifies that a tool is safe for use over a whole shift. When an employee takes a tool from our stores they are told of the risks associated with the item.

At Naval Ships we have invested in new equipment so that 98% of the tools at our Govan site and 95% at Scotstoun now carry the green label. Tools are inspected regularly to make sure they comply with our standards.

### Submarines

#### Highlights for 2006

- Reduced lost time through accidents by 21%.
- Updated our health and safety policies so all employees are required to wear an oxygen level monitor when entering a confined space.
- Conducted a smoking cessation programme in conjunction with the NHS, which included free counselling and medication and trained trade union representatives as stop smoking advisors.
- Employees raised £16,971 for 29 local charities through our Give as You Earn Scheme.
- Launched a liaison group and community newspaper to target and report our local community investment activities.
- Launched the PRIDE campaign to encourage employees to engage with the local community.
- Completed a partnership with the Northwest Regional Development Agency to re-skill our workforce (the partnership delivered 22,523 training hours over two years).
- Gained planning permission to install a wind turbine or series of wind turbines to power lights and computers in areas such as the main reception foyer at the shipyard.
- Employees were awarded the Linda Wilkins memorial award for community involvement at the Charity Challenge awards ceremony.

#### Building a floating hospital

Many remote communities in the Peruvian Amazon have no access to medical services. Five years ago, Naval Ships' apprentices converted a former Royal Navy boat into

the Amazon Hope, a floating hospital which extended a lifeline to these communities. This year, Submarines employees helped create a sister medical vessel for the region, Amazon Hope 2.

First our employees and the local community raised £158,000, exceeding the £100,000 needed by the Vine Trust to make the Amazon Hope 2 conversion happen.

Our apprentices could then begin refitting the vessel at our shipyard. They created an operating theatre, a dentistry room and accommodation space for nurses and visiting medical teams. Naval Ships funded architect Tom Dunn to travel to Peru to bring the original Amazon Hope up to the same standard as her new sister boat.

The finished Amazon Hope 2 was exhibited at the International Festival of the Sea in Portsmouth, where she was re-commissioned by HRH Princess Royal and visited by over 25,000 people. Members of the team involved in the refit then helped deliver the boat to its final destination 11,000 miles away in Peru. The crew braved 8ft waves and 40c temperatures to bring the Amazon Hope 2 to its home port of Iquitos.

We are now collaborating with Barrow Borough Council to send 20 pupils from local secondary schools to see the boats at work in Peru, in August 2007.

Left: Naval Ships is leading Group efforts to reduce risks from working in confined spaces and from hand-arm vibration syndrome (HAVS).

Right: Submarines employees helped to build Amazon Hope 2, a floating medical vessel for remote communities in the Peruvian Amazon.

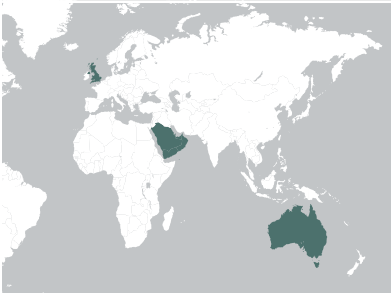


# Customer Solutions & Support

## Principal operations

Provides partnered, through-life support and capability solutions to the UK MoD and manages the businesses in Saudi Arabia and Australia.

## Main operating locations



## Major markets

UK/Europe, Middle East, Australia

## Share of 2006 Group Sales



**£3,180m**  
**22%**

## Number of employees

**14,600**

## Customer Solutions & Support

### Highlights for 2006

- Completed our four year project to create vocational standards for skilled trades in Saudi Arabia.
- Helped school students to set up and run business ventures as part of the Young Enterprise Scheme.
- Achieved the international health and safety standard OHSAS 18001 at our CS&S International UK Offices and commenced the programme for assessment in all our remaining UK business.
- Introduced new safety, health and environment (SHE) 'passport' training for all CS&S MASS employees as well as SHE training specifically for senior executives.
- Introduced a distance learning health and safety course for our international businesses including translating into Arabic to include our Saudi employees and members of the RSAF.
- We have undertaken an Occupational Health baseline review led by an independent occupational physician to identify our key OH areas for improvement going forward.
- Held a conference with Greenpeace to discuss the green disposal of ships. The London conference in May was the first major UK forum on the subject and brought together stakeholders from a range of backgrounds.
- We have undertaken a shadow BITC benchmark survey and are in the process of analysing the output and recommendations. We plan to develop some initiatives to improve various aspects of CR going forward.
- Sponsored ten children in impoverished third world countries through the Workplace Giving Scheme in Australia.
- CS&S Australia employees partnered with external businesses and suppliers to design and build a sensory garden for the disabled residents at the Klemzig Residential Care Home in South Australia.

### Helping a school reach specialist school status

Moor Park High School is located in one of the most challenging inner city areas of Preston, UK. In 2006, the school applied for Business and Enterprise specialist status in a bid to make its pupils more employable. Business and Enterprise is a UK education standard which helps students develop employment skills and progress to higher education. We donated £10,000 to the school to help its application. We chose to support Moor Park's bid as we felt that specialist status would make a real difference to the school. We were also impressed with its inclusive environment.

Now Moor Park has achieved specialist status it has secured funds to extend the school facilities to benefit both its pupils and the local community. In addition we have supported the school's business and enterprise activities. This has included offering leadership training for teachers and providing pupils with opportunities to attend a workshop to give them experience of a business environment. We have also given advice to the school on branding, communication and strategy. Our schools road show has also visited the school to get the students involved in science and engineering projects.

The deputy head teacher at Moor Park Business and Enterprise School, Phil Jagggers, said "we appreciate the support given by BAE Systems and look forward to developing our relationship. Specialist School status will provide Moor Park with an opportunity to develop the innate enterprising spirit that many of our pupils exhibit, providing a focus for raising standards."



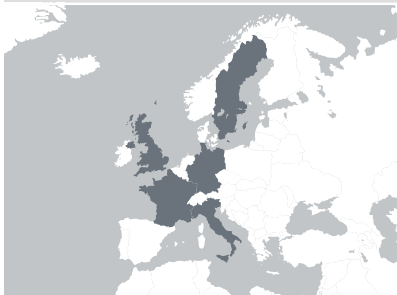
Left: CS&S chose to support Moor Park's bid for specialist status because it would make a real difference to the school.

## Integrated Systems & Partnerships

### Principal operations

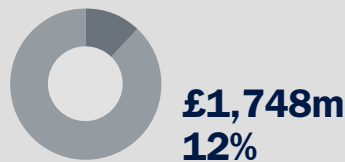
A portfolio of high-technology defence systems businesses comprising the wholly-owned Integrated System Technologies and Underwater Systems businesses, together with a 37.5% interest in the pan-European MBDA joint venture, a 20.5% interest in Saab of Sweden and a 50% interest in the Gripen International joint venture.

### Main operating locations



Major markets  
UK/Europe

### Share of 2006 Group Sales



### Number of employees

**10,500**

### Integrated System Technologies (Insyte)

#### Highlights for 2006

- Creation of an Insyte TU Steering Group to help focus on CR.
- Formation of a joint working group to co-ordinate and prioritise more effective lobbying arrangements on behalf of Insyte.
- Continuation of active health monitoring and surveillance programme, OH rehabilitation, back to work and specialist support.
- Participation in the WISE (Women into Science and Engineering) scheme.
- Insyte together with its employees have raised over £245,000 for various charities during 2006.
- Participation in the 'Take your Daughters and Sons' day on April 27th.
- Review of site facilities to ensure that employee and visitor religious needs are being accommodated e.g. provision of prayer rooms.
- Further increases in the number of employees taking advantage of more flexible working arrangements as part of Insyte's initiative on work life balance.

#### Improving the workplace for all our employees

Workforce diversity was a focus for Insyte during 2006. In response to diversity metrics concerning retention of key demographic groups, we appointed an HR manager, with a specific responsibility for our graduate and technical apprentice programmes. Employee retention is also expected to improve as a result of training 16 new Respect at Work contacts throughout the year. They will act as an alternative point of contact for employees, offering support and guidance in suspected cases of discrimination, harassment or bullying in the workplace.

A review of our employee benefits schemes has taken place to ensure they cater for the complete range of needs of all our employees. In addition, and in response to our 'Ask the Board' and other employee

feedback mechanisms, Insyte have introduced a new All Employee Recognition Award Scheme designed to deliver more equity within the nomination procedure by allowing any employee within the business the opportunity to recommend a fellow employee for recognition.

Employee opinions were also key in initiating a review of our Long Service Award Recognition Scheme. The feedback received on existing policies indicated a failure to recognise certain key milestones in service and consequently a more balanced and equitable arrangement was developed across the business.

### Underwater Systems

#### Highlights for 2006

- Launched a driving safety scheme including practical and theory sessions for drivers.
- Introduced a good spot safety campaign.
- Supported the Bike to Work scheme.

UWS established its Working Party for Health (WPFH) in 1996 to encourage employees to participate in health promotion activities across the site and take responsibility for their health. The WPFH celebrated ten years last year and as part of the anniversary celebrations, organised a Wellbeing Day at Underwater Systems. Employees were invited to meet and have taster sessions with a range of practitioners and therapists.

The WPFH has organised a range of activities including voluntary general health checks, lunchtime talks, drug and alcohol awareness sessions and smoking cessation groups. In addition the group organises blood donation sessions and facilitates Pilates and massage sessions each week.

Left: Insyte participated in the WISE (Women into Science and Engineering) scheme.

Right: Underwater Systems' Working Party for Health has helped employees to lead healthier lifestyles for the last decade.



# HQ and other businesses

## Principal operations

Comprises the regional aircraft asset management and support activities, head office and UK shared services activity, including research centres and property management.

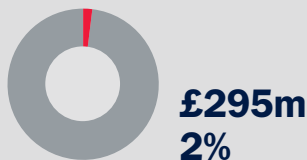
## Main operating locations



## Major markets

UK

## Share of 2006 Group Sales



## Number of employees

**2,300**

## Head office

### Highlights for 2006

- Sponsorship of the UK MoD's Christmas Box scheme which provides 25,000 Christmas gift boxes for all UK troops on overseas exercise.
- Sponsorship of a Christmas concert for UK troops in Basra, Iraq featuring Welsh opera star, Katherine Jenkins.
- Sponsorship of each of the UK Armed Forces Sports Boards enables service personnel to further pursue sporting triumph.
- Sponsorship of the Royal International Air Tattoo helps the organisers stage this unique celebration of aviation for over 150,000 members of the general public on an annual basis.
- Support of several charities through our Relationship Charity Programme, giving £100,000 to each over three years. This guaranteed sum helps the charity to plan ahead and commit to a specific project. The charities we supported in 2006 were: Leukaemia Research, St John Ambulance, the No Way Trust, Age Concern, and the US Juvenile Diabetes Research Foundation.

### Committed to preserving our global heritage

BAE Systems is keen to commemorate the activities of its predecessor companies throughout the world. The company recently supported the Tank Museum at Bovington, Wiltshire and the Royal Naval Museum at Portsmouth in addition to the Pearl Harbor Memorial Museum in Hawaii.

Our long-term support for the Imperial War Museum at Duxford in Cambridgeshire has helped to build a completely new museum to tell the story of British aviation.

AirSpace will enable BAE Systems' vast and valuable collection of UK aviation artefacts, photographs, films and documents to be suitably preserved and displayed for visitors to enjoy for years to come.

## Regional Aircraft

### Highlights for 2006

- Donated £10,030 to 18 local community groups.
- Nine employees took part in the Glasgow Women's 10K run, raising £2,500 for the Stillbirth and Neonatal Death Society.
- Donated two model training aircraft to the Air Training Corp, an activities organisation for 13-18 year olds.
- Launched a modern apprentice programme and recruited three technical and one commercial apprentice

### Supporting education

Regional Aircraft invests in education to help develop the next generation of engineers from primary school students to university postgraduates.

In June, nine Regional Aircraft employees brought the BAE Systems' schools roadshow to four schools near our sites. This included workshops and a theatre performance designed to get children excited about science and engineering.

Twenty-five secondary school students spent a week getting hands-on experience of an engineering career through work placements at one of our sites.

Regional Aircraft has strong links with universities. Our employees lecture on the aerospace industry at Glasgow and Strathclyde Universities and help students with their final year engineering projects. They also run a three-day course in Aircraft Integrated Design.

We are donating one of our avionics systems rigs to Cranfield University. This will improve the university's postgraduate research and teaching capabilities. Cranfield University aim to have the rig fully installed by May 2007.

Left: Regional Aircraft invests in education to help develop the next generation of engineers from primary school students, through apprentices to university postgraduates.

Right: Aircraft on display in Airspace, the new museum at Duxford, Cambridgeshire.



# Performance summary

We collect data on ethics, diversity, environment, health and safety and community investment to help us monitor our CR performance and identify areas for improvement.

	2004	2005	2006	page	
<b>Economic</b>					
Revenue <sup>1</sup>	£8,817m	£11,019m	<b>£12,333m</b>		
Operating profit <sup>2</sup>	£656m	£761m	<b>£1,054m</b>		
Dividend paid in year	£281m	£315m	<b>£346m</b>		
Wages and salaries <sup>1</sup>	£2,469m	£2,989m	<b>£3,274m</b>		
Pension costs <sup>1</sup>	£226m	£233m	<b>£253m</b>		
Employee numbers <sup>1</sup>	73,300	80,000	<b>79,000</b>		
<b>Health and safety<sup>3</sup> (per 100,000 employees)</b>					
Major accidents	61	55	<b>47</b>	29	
Days lost to work-related injuries	9,126	8,774	<b>10,204</b>	31	
Total injuries to all employees	7,969	6,009	<b>4,788</b>	30	
<b>Environment<sup>3,4</sup></b>					
Energy use (Gwh)	1,321	1,767	<b>1,742</b>	27	
CO <sub>2</sub> emissions (million tonnes)	0.49	0.58	<b>0.57</b>	27	
Waste ('000 tonnes)	345	57	<b>105</b>	28	
Waste recycled ('000 tonnes)	67	37	<b>67</b>	28	
Volatile organic compound emissions (tonnes)	241	610	<b>742</b>	28	
Water use (million m <sup>3</sup> )	46	36	<b>40</b>	26	
<b>Ethics</b>					
Ethics enquiries	616	367	<b>410</b>	25	
<b>Diversity</b>					
Gender diversity:	Male employees	80%	81%	<b>80%</b>	32
	Female employees	20%	19%	<b>20%</b>	32
Ethnic diversity:	White	92%	88%	<b>87%</b>	32
	Non-white	8%	12%	<b>13%</b>	32
Age diversity <sup>5</sup> :	under 25	5.9%	6.6%	<b>6.6%</b>	33
	26 to 35	14.7%	18.4%	<b>18.2%</b>	33
	36 to 49	40.8%	43.3%	<b>42.6%</b>	33
	50 to 59	20.8%	25.3%	<b>25.9%</b>	33
	60+	5.2%	6.4%	<b>6.7%</b>	33
<b>Community investment</b>					
What we have contributed (£m)	1,100,000	10,525,78	<b>8,223,160</b>	34	

1 Excluding equity accounted investments

2 Including share of equity accounted investments

3 The increases shown for 2006 reflects the expansion of our business in the US in 2005 to include the former UDI and ship repair business (2006 is the first full reporting year). This particularly affects the safety risk profile and use of resources.

We will be aiming to reduce the impact of each individual business year on year

4 Recalculated to include 2005 acquisitions

5 2003 and 2004 figures do not include data for Saudi Arabia



To view our performance on-line visit [www.baesystems.com](http://www.baesystems.com)

# Ethics

## Ethics

### Ethics enquiries

	2004	2005	2006
Formal ethics enquiries – UK and Rest of World	42	31	<b>62</b>
Formal ethics enquiries – US	574	336	<b>348</b>
<b>Total enquiries</b>	<b>616</b>	<b>367</b>	<b>410</b>

### Trend

The number of ethics enquiries received through our ethics officers, helplines and e-mail address was 410. This was an increase of 43 from 2005 when we received 367 enquiries.

### Dismissals

	2004	2005	2006
Dismissals for reasons relating to unethical behaviour – UK and Rest of World			<b>28</b>
Dismissals for reasons relating to unethical behaviour – US			<b>22</b>
<b>Total dismissals</b>			<b>50</b>

### Explanation

The increase in the number of reports received in the UK and US this year is related to the increased awareness of the helpline and ethical policies and standards as a result of online and DVD training for all employees which took place in 2006. In particular the number of reports to the UK and ROW helplines doubled in 2006 – from 31 in 2005 to 62. This is as a direct result of the newly introduced online training for all employees which has raised awareness levels of the Helpline.

### Types of calls to ethics helpline – UK and Rest of World (%)



### Types of calls to ethics helpline – US (%)



# Environment

## Introduction

**Our environmental impact is related to the nature of our operations, the size of our footprint and the scale of throughput.**

Given the changes to our operating profile and volume of production over the last two years, particularly in the US, we are presenting our environmental data separately for the UK and US regions. This is intended to provide further transparency and improve the explanation of trends and factors affecting impacts.

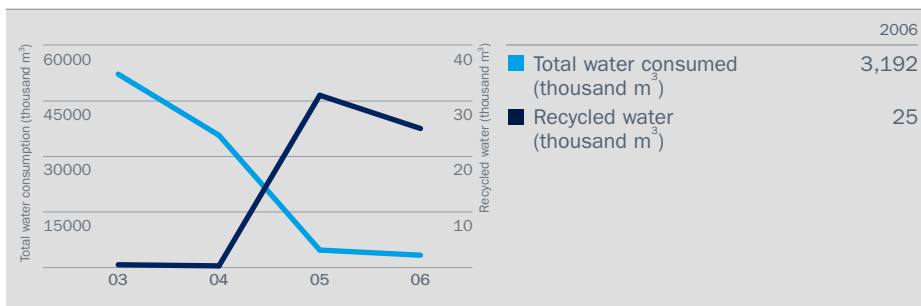
For the current profile of our operations we have four years of data for the UK and two years for the US. Our operations in other regions have relatively small environmental impacts and represent less than 5% of the overall total for the company.

Going forward we will provide further transparency by relating the environmental impacts to each specific business and type of operation. Our UK business continues to show overall improved environmental management. Certain projects and stages of build will always have a disproportionate effect on our environmental data. For example, the impact of the remediation of the former Chorley site in 2003 and 2004 can be seen on the amounts of waste generated and recycled. Major site waste clearance at Towcester and Great Baddow also disproportionately increased the amount of waste disposed during 2006. Water consumption will also increase at particular stages of ship and submarine build when the platforms are floated in the docks.

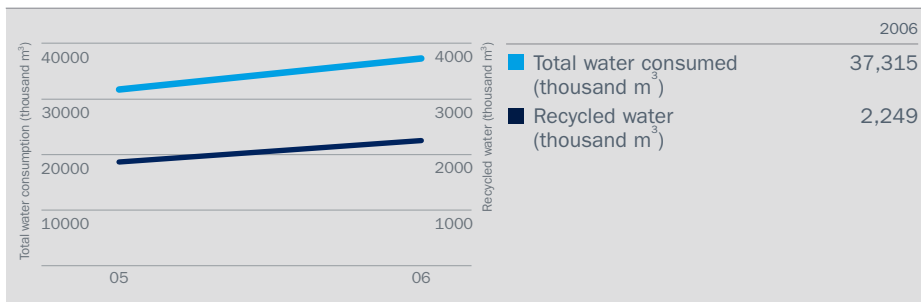
Our production throughput in the US has increased significantly in some areas, particularly in the production for the Bradley fighting vehicles and this affects all aspects of environmental impact.

## Water use

### UK

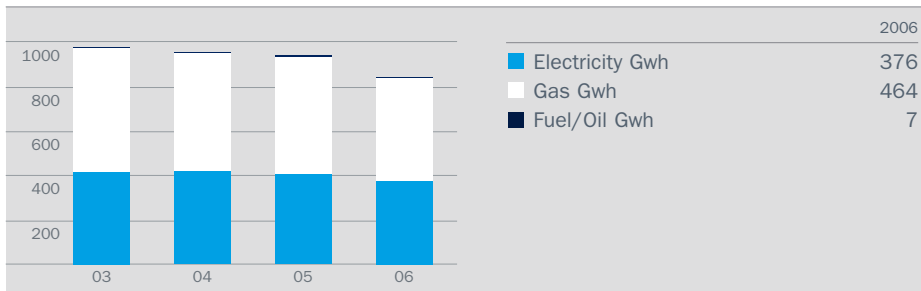


### US

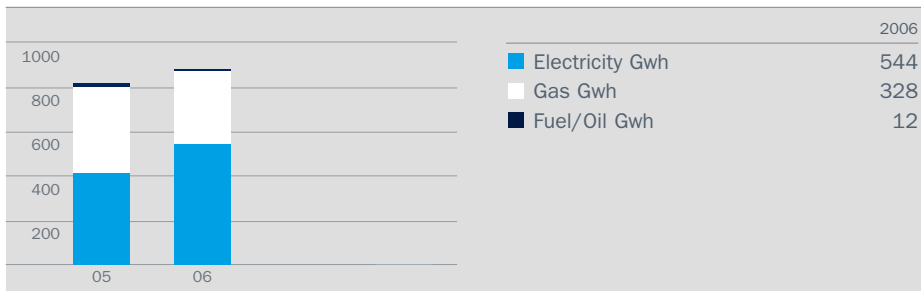


## Energy consumption

### UK

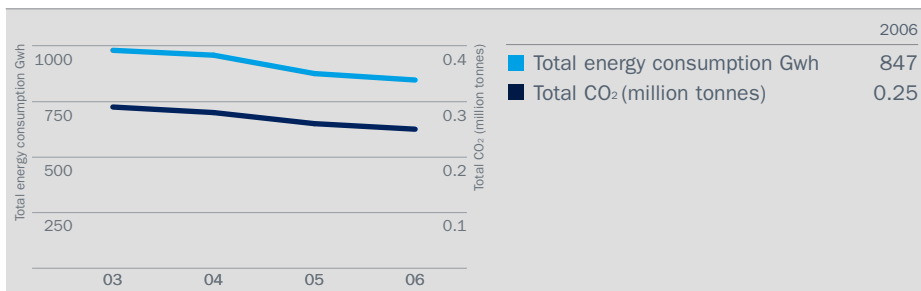


### US

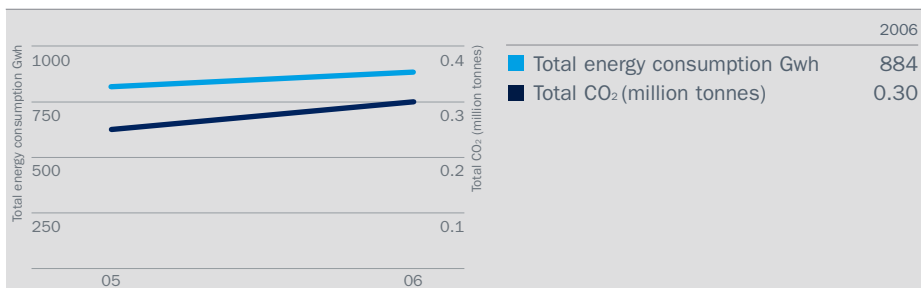


## Total energy use

### UK



### US

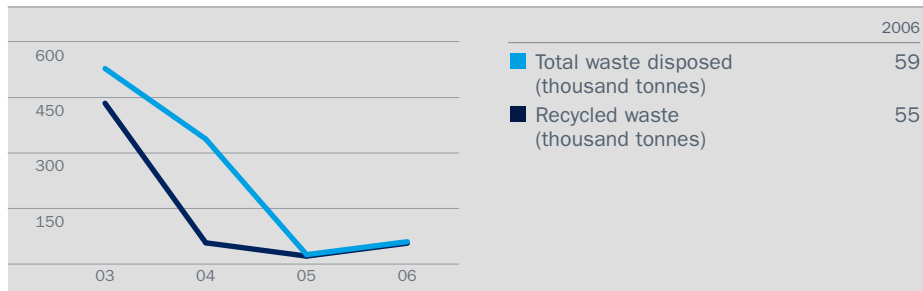


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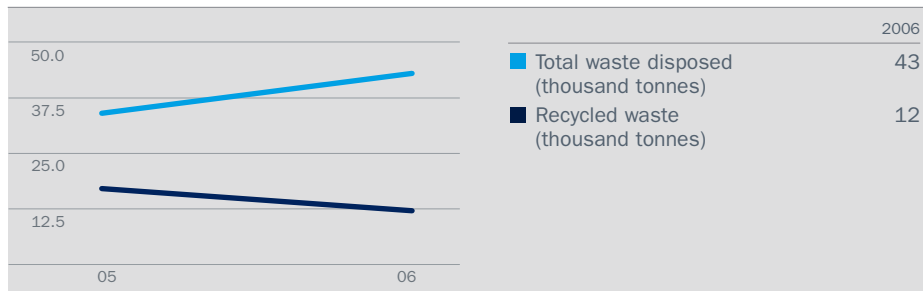
## Environment (continued)

### Waste

#### UK

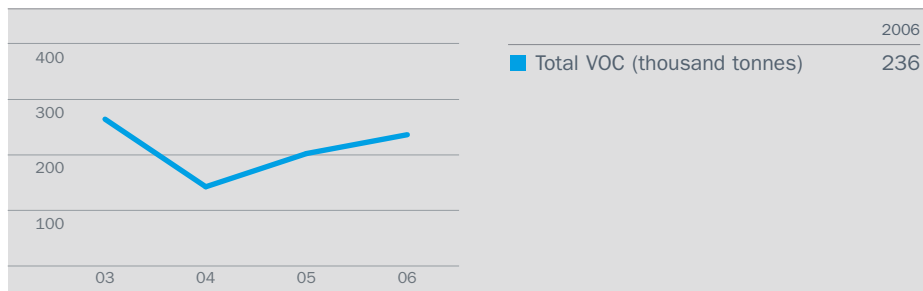


#### US

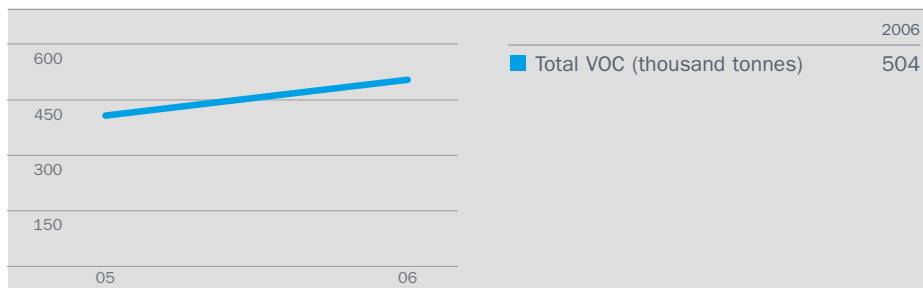


### Volatile organic compounds

#### UK



#### US



# Health and safety

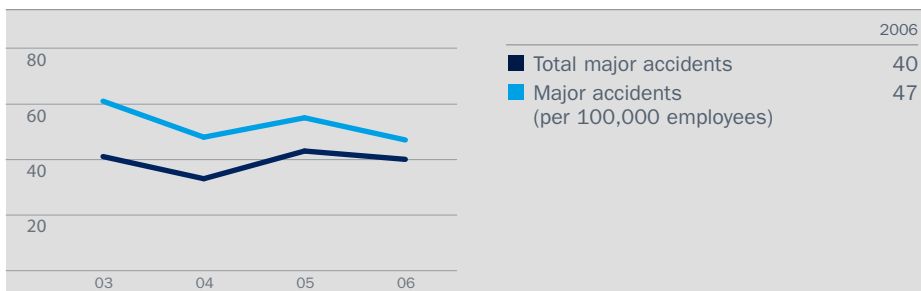
## Introduction

2005 and 2006 figures include the former United Defence Industries business and the ship repair yards which involve heavy manufacturing and increases the overall number of major accidents compared to 2004.

Overall the total number of injuries continues to decrease but the days lost per work related injury has shown an increase. We are addressing this through a pro-active rehabilitation programme in partnership with our insurance providers.

Primary causes of injury continue to be manual handling, collision with objects and slips and trips. These issues are being addressed through the development of common standards and an audit programme supported by the safety regulators.

## Major accidents



Major injuries as defined under the UK Reporting of Injuries, Diseases and Dangerous Occurrences Regulations (RIDDOR)

	2003	2004	2005	2006
UK major accidents	24	24	15	<b>21</b>
UK rate per 100,000 employees	68	65	39	<b>54</b>
US major accidents	9	4	27	<b>16</b>
US rate per 100,000 employees	38	17	83	<b>41</b>
Aus major accidents	0	2	0	<b>1</b>
Aus rate per 100,000 employees	0	53	0	<b>35</b>
KSA major accidents	8	3	1	<b>2</b>
KSA rate per 100,000 employees	163	65	22	<b>44</b>
<b>Total major accidents</b>	<b>41</b>	<b>33</b>	<b>43</b>	<b>40</b>
<b>Total rate per 100,000 employees</b>	<b>61</b>	<b>48</b>	<b>55</b>	<b>47</b>

UK manufacturing industry average 2005-06: 180.3 per 100,00 employees

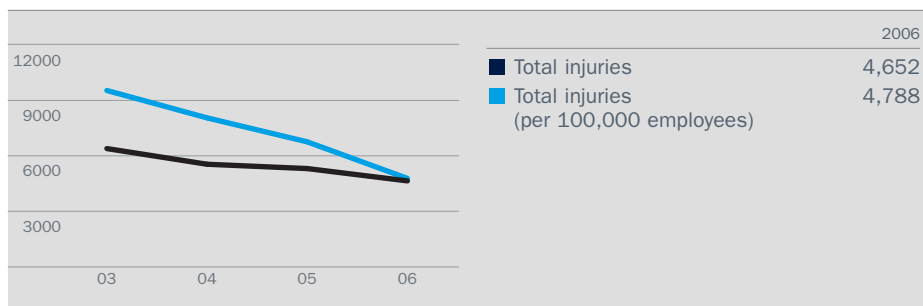
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### Health and safety (continued)

#### Cause of injury (%)

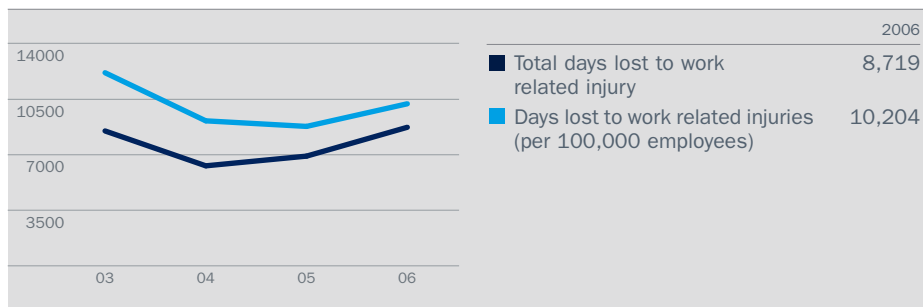


#### Total injuries to all employees



	2003	2004	2005	2006
UK total injuries	5,862	4,931	4,305	<b>3,409</b>
UK rate per 100,000 employees	16,683	13,308	10,704	<b>8,745</b>
US major injuries	263	391	751	<b>976</b>
US rate per 100,000 employees	1,096	1,629	2,315	<b>2,518</b>
Aus. major injuries	51	123	161	<b>137</b>
Aus. rate per 100,000 employees	1,357	3,282	5,902	<b>4,847</b>
Saudi major injuries	263	129	143	<b>130</b>
Saudi rate per 100,000 employees	5,351	2,803	3,186	<b>2,869</b>
<b>Total major injuries</b>	<b>6,403</b>	<b>5,554</b>	<b>5,320</b>	<b>4,652</b>
<b>Total rate per 100,000 employees</b>	<b>9,550</b>	<b>8,067</b>	<b>6,768</b>	<b>4,788</b>

## Days lost to work related injuries

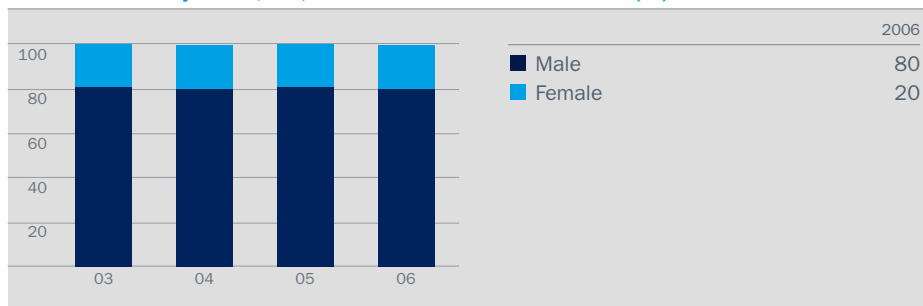


	2003	2004	2005	2006
UK days lost work-related injuries	6,870	4,529	3,532	<b>3,977</b>
UK rate per 100,000 employees	19,553	12,223	8,782	<b>10,193</b>
US days lost work-related injuries	1,603	1,130	2,952	<b>4,434</b>
US rate per 100,000 employees	6,679	4,708	9,096	<b>11,441</b>
Aus days lost work-related injuries	14	716	176	<b>60</b>
Aus rate per 100,000 employees	467	19,103	6,452	<b>2,123</b>
KSA days lost work-related injuries	–	115	267	<b>248</b>
KSA rate per 100,000 employees	–	2,499	5,948	<b>5,474</b>
<b>Total days lost work-related injuries</b>	<b>8,487</b>	<b>6,283</b>	<b>6,896</b>	<b>8,719</b>
<b>Total rate per 100,000 employees</b>	<b>12,167</b>	<b>9,126</b>	<b>8,774</b>	<b>10,204</b>

## Diversity

### Gender diversity

#### Gender diversity – UK, US, Australia and Saudi Arabia (%)



\*2003 and 2004 data does not include Saudi Arabia.

	UK	US	AUS	Saudi	Total
2003 male	31,668	16,739	2,215	–	<b>50,622</b>
2003 female	5,011	6,630	443	–	<b>12,084</b>
2004 male	31,953	17,731	2,132	–	<b>51,816</b>
2004 female	5,021	7,261	433	–	<b>12,715</b>
2005 male	22,956	26,756	2,208	5,106	<b>64,026</b>
2005 female	4,784	9,677	452	32	<b>14,945</b>
2006 male	27,164	25,774	2,305	4,536	<b>59,779</b>
2006 female	4,380	9,673	466	20	<b>14,539</b>

#### Trend

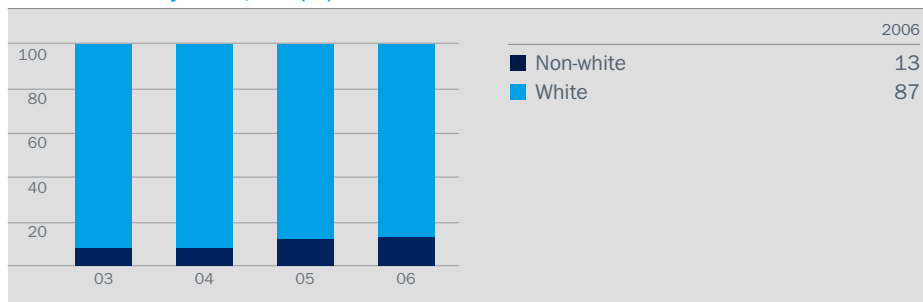
In 2006 20% of employees were female. This figure is an increase of 1% on 2005

#### Explanation

We are working to change the demographics within our business but recognise that this will occur slowly over time. We have a number of initiatives (see page 12) in place to increase the number of women across our global businesses. In 2007 this will focus on broadening the diversity of the applicant pool from which we recruit graduates and apprentices whilst ensuring equal opportunities for all employees.

### Ethnic diversity

#### Ethnic diversity – UK, US (%)



#### Trend

In the UK and US 13% of employees come from an ethnic minority background. This figure is an increase of 1% from 2005.

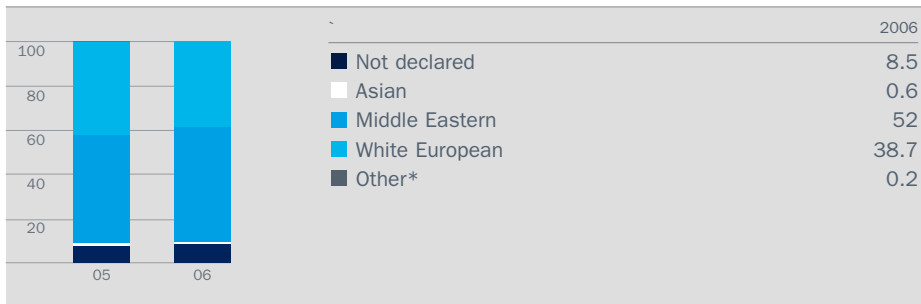
#### Explanation

We are working to change the demographics within our business but recognise that this will occur slowly over time. We have a number of initiatives (see page 12) in place across our global businesses. In 2007 this will focus on broadening the diversity of the applicant pool from which we recruit graduates and apprentices whilst ensuring equal opportunities for all employees.

	UK	US	Total
2003 white	36,296	19,162	<b>55,458</b>
2003 non-white	383	4,207	<b>4,590</b>
2004 white	36,560	20,470	<b>57,030</b>
2004 non-white	412	4,522	<b>4,934</b>
2005 white	34,391	28,282	<b>62,673</b>
2005 non-white	349	8,151	<b>8,500</b>
2006 white	31,183	27,400	<b>58,583</b>
2006 non-white	361	8,047	<b>8,409</b>

## Ethnic diversity

### Ethnic diversity – Saudi Arabia (%)



\*Other' includes Oriental/SE Asian, black African and black Caribbean.

#### Trend

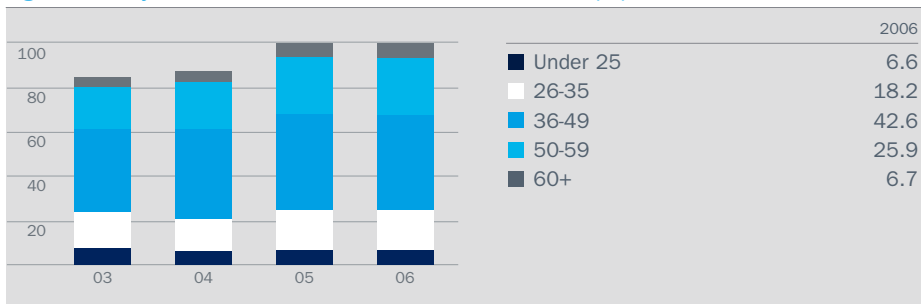
In Saudi Arabia the majority (52%) of employees are Middle Eastern. White Europeans make up another 39% of the workforce.

#### Explanation

A key element of our commitment to our Saudi customers and an important part of the home market strategy in the Kingdom of Saudi Arabia, is our Saudiisation programme. This delivers both transfer of expertise to the Saudi people and the transfer of technology to Saudi industries. We will continue to monitor demographics in our Saudi Arabian business as part of this ongoing programme.

## Age diversity

### Age diversity – UK, US, Australia and Saudi Arabia (%)



	UK	US	AUS	Saudi	Total
2003 under 25	10	5	26.2	–	<b>7.5</b>
2003 26-35	19.3	16	43.8	–	<b>16.2</b>
2003 36-49	45.6	45	18.5	–	<b>37.6</b>
2003 50-59	21.9	25	3.2	–	<b>19</b>
2003 60+	2.9	9	8.3	–	<b>4.6</b>
2004 under 25	9.3	3	8.8	–	<b>5.9</b>
2004 26-35	18.6	13.4	25	–	<b>14.7</b>
2004 36-49	45.6	48.6	43.3	–	<b>40.8</b>
2004 50-59	23.1	25.2	19.1	–	<b>20.8</b>
2004 60+	3.5	9.8	3.8	–	<b>5.2</b>
2005 under 25	9.5	3.87	10	4.4	<b>6.6</b>
2005 26-35	17.2	17.96	25.2	26.5	<b>18.4</b>
2005 36-49	44.8	41.8	44.4	43.2	<b>43.3</b>
2005 50-59	24.4	27.01	17.4	22.4	<b>25.3</b>
2005 60+	4.1	9.36	3	3.5	<b>6.4</b>
2006 under 25	10.1	3.79	8.6	2.1	<b>6.6</b>
2006 26-35	16.3	18.45	25.9	24.2	<b>18.2</b>
2006 36-49	44.5	40.43	43.2	46.2	<b>42.6</b>
2006 50-59	24.8	27.78	18.5	24.3	<b>25.9</b>
2006 60+	4.3	9.56	3.8	3.2	<b>6.7</b>

#### Trend

In 2006 the majority of our employees (42.6%) were aged between 36 and 49. The number of employees aged under 25 has remained constant at 6.6%.

#### Explanation

We continue to monitor age diversity across the business to assess trends and ensure business continuity and skills transfer.

## Community

### Community investment

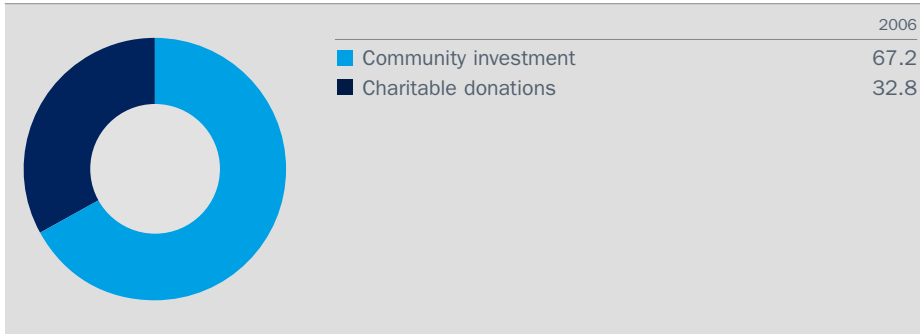
#### What we contribute to (%)



#### Trend

In 2006, our total community investment was £8,223,160 compared to £10,525,731 in 2005. This figure includes cash and in-kind donations to charity as well as our direct support for communities and education across the world.

#### Focus of contribution (%)



# External assurance statement

BAE Systems has commissioned The Corporate Citizenship Company to provide it with external assurance and commentary on its Corporate Responsibility Report 2006. BAE Systems' management has prepared the report and is responsible for its contents. Our objectives were to review and advise on aspects of its contents and presentation, to conduct selected checks to underlying corporate records, and to provide this statement for which we have sole responsibility. A full statement of our external assurance and commentary is available at [www.baesystems.com](http://www.baesystems.com) including details about The Corporate Citizenship Company, our relationship with BAE Systems and the assurance process we have adopted. This statement summarises our principal findings.

### Our opinion

In our opinion, the report provides a fair and balanced representation of the progress BAE Systems is making in living out its commitments to corporate responsibility. Where we believe significant gaps exist in available performance data and stakeholder views on material issues, we identify them in our commentary below. In forming our opinion and making our comments, we have had regard to the principles underlying the international assurance standard AA1000 ([www.accountability.org.uk](http://www.accountability.org.uk)) notably concerning materiality, completeness and responsiveness. We have also had regard to the reporting guidance for content and the principles for defining quality contained in GRI's G3 sustainability reporting guidelines. ([www.globalreporting.org](http://www.globalreporting.org)).

### Commentary

A corporate responsibility report should explain how a company impacts on society, looking at all the important economic, social and environmental concerns of its stakeholders. It should show how crucial decisions are made, and differing interests balanced. Honest about shortcomings, it should demonstrate how the organisation is responsive, by listening, learning and improving.

Against this goal, we believe BAE Systems 2006 report demonstrates continued progress in the company's reporting of its corporate responsibility practices across all aspects of its business. The company remains ahead of its sector in its reporting and outperformed in all but one component of the Dow Jones Sustainability Index.

This year's report provides an account of activity by each of BAE Systems' five business groups. This is particularly valuable

given the company's reorganisation over the past year. Building on last year's stakeholder research BAE Systems has opened up to more external parties, for example through the roundtable discussion on its environmental impacts, discussed in the "debating the future" section. BAE Systems has also made efforts to be more forward-looking in its corporate responsibility activities. It has taken steps to lay out its corporate responsibility plans and agenda for 2007 to 2012, which is to be welcomed.

### Looking ahead

In our opinion the following issues should be addressed if BAE Systems is to meet best practice standards for reporting materiality, completeness and responsiveness:

### Materiality

Presenting the report by business group helps to give a better understanding of the scope and focus of BAE Systems' different business activities. We believe readers would benefit from the company fully accounting for the impacts of each group. This would allow the company to identify the most important impact each business has relevant to its own operations. A leading approach would be to publish performance targets in relation to each.

North American business now represents approximately one third of all sales and over one third of the workforce, yet the limited information given about operations and impacts there is not in keeping with the importance to the company as a whole. In part, the limited information reflects the rapid growth of the US business. Future reports would be materially improved if this imbalance were addressed.

BAE Systems states in its core values its commitments to its customers. However, there is little discussion of its principal customers, or how the company maintains relationships and delivers high levels of service to them. We believe understanding this is material to understanding the business. Future reports should explain to readers what it means to do business in six "home markets" with exports to numerous countries, while the sale of its products is restricted by national authorities.

### Completeness

Looking at the range of topics covered, this year's report addresses social impacts well, although this would be strengthened by stating the strategic aims of employee and community activities. BAE Systems has been reporting on its environmental impacts for over five years. We look forward

to future reports building on initiatives currently underway to show how the company is contributing to the UK's national sustainable development objectives.

We believe the report would be more complete if it explained BAE Systems' economic impacts. Not only is BAE Systems a large employer, but it is a large purchaser of goods and services in its principal markets. Detailing its direct and indirect economic impacts would help to give a more complete picture of the company. In keeping with this and with last year's recommendations, future reports should give more information about its relationships with suppliers.

### Responsiveness

As with last year, this report addresses challenging issues in its "key issues for our stakeholders" section. BAE Systems briefly states its position regarding press coverage of some allegations of misconduct. BAE Systems has stated elsewhere that it is unable to comment on this situation while investigations are on-going. Nonetheless, given the extent of concern expressed, including public statements from institutional and other investors, we believe readers would expect to see a fuller expression of the company's position.

The climate change roundtable highlighted the need for BAE Systems to develop an effective climate change strategy. At present it captures data about greenhouse gas emissions, but it should make set clear targets for their reduction. Because of the nature of its products and their production cycles, which are not always predictable, there are challenges to setting annual targets, but it is important to move in this direction if the company is to meet the expectations of stakeholders.

Other issues in which readers of corporate responsibility reports are expressing interest include: detailing membership of trade associations and lobbying activities; providing information about targets not met; and contributions to governments through tax, offset agreements and partnerships.

9 March 2007



[www.corporate-citizenship.com](http://www.corporate-citizenship.com)

# Can't find what you are looking for?

For full information on all aspects of our Corporate Responsibility agenda, policy statements and information on how we operate and our responsibilities as a defence company, see our detailed CR website at: [www.baesystems.com/corporateresponsibility](http://www.baesystems.com/corporateresponsibility)

↳ For further CR information

This report is only one of many sources of information about our company. The following information is also available on our website.

- For an account of our year's financial performance, products and services sold and highlights on performance read our Annual Report and Accounts available at [www.baesystems.com](http://www.baesystems.com)
- For how we manage our business and our full corporate governance statement visit [www.baesystems.com/investors](http://www.baesystems.com/investors)
- For dedicated information for shareholders including investor presentations and regulatory announcements visit [www.baesystems.com/investors](http://www.baesystems.com/investors)

Annual Report available

Governance Statement

Information for shareholders



## Feedback

We welcome feedback, both positive and negative, on any aspect of our corporate responsibility reporting and performance. Email us at [crfeedback@baesystems.com](mailto:crfeedback@baesystems.com)

For more information contact:

### Dr Deborah Allen

Director of Corporate Responsibility  
Telephone +44 (0)1252 383 388  
Email [deborah.allen@baesystems.com](mailto:deborah.allen@baesystems.com)  
or [crfeedback@baesystems.com](mailto:crfeedback@baesystems.com)

### Leigh Munro

Corporate Responsibility Manager  
Telephone +44 (0)1252 385 168  
Email [leigh.munro@baesystems.com](mailto:leigh.munro@baesystems.com)  
or [crfeedback@baesystems.com](mailto:crfeedback@baesystems.com)



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**BAE Systems plc**

6 Carlton Gardens  
London SW1Y 5AD  
United Kingdom  
Telephone +44 (0)1252 373232

Registered in England and Wales No. 1470151

[www.baesystems.com](http://www.baesystems.com)