

Making progress



Contents

Chief Executive's Statement	1	This is our eighth Corporate Responsibility (CR) Report. Here we discuss our priorities for CR and how we are performing. We are working hard to move from a CR strategy serving business needs to a business strategy conducted responsibly.
Our Strategy	2	
Stakeholder Engagement	6	
CR Panel	8	Throughout the report we have aimed to be as clear as possible about our approach to CR and to report setbacks as well as progress made. We believe this helps to create openness, maintain trust in our business and improve relationships with all stakeholders.
Business Conduct	10	We are committed to giving further evidence to stakeholders on how we are implementing our commitment to being a responsible company. To address this we have undergone an independent assurance process on our CR Report. We have sought feedback from a panel of CR experts on our strategy, progress and reporting.
Health, Safety and Environment	16	
Workplace	26	
Education and Community	30	
Assurance Statement	32	Assurance Following a tender process, Deloitte LLP were appointed to provide independent assurance of our CR Report on the following basis: - Limited assurance of the CR Report compilation process - Reasonable assurance of our description of the Woolf implementation programme. Limited assurance requires assurers to confirm that they have not found anything to make them believe our reporting is materially misstated. Reasonable assurance goes to a further level of detail and auditing and requires assurers to confirm that they believe the content of the report is fairly stated. Deloitte's statement is published on page 32.
Performance Summary	33	

External review

For the second year, we have convened a panel of experienced CR practitioners to provide feedback on our strategic approach and identify areas for improvement. Their review and statement is on pages 7-9.

Report process

The data and performance measures in this report cover January – December 2008.

Qualitative information and quantitative data for the report are provided by nominated points of contact across our business.

Quantitative data is recorded on Company systems. Content and data are reviewed at BAE Systems plc.

Data covers major operations globally, excluding those acquired during the year.

We aim to align our reporting with recognised standards over a three year period.

Your feedback

We welcome feedback, both positive and negative, on any aspect of our Corporate Responsibility reporting and performance. Email us at crfeedback@baesystems.com

Who we are and what we do

BAE Systems, with 106,400 employees¹ worldwide, delivers a full range of systems and services for air, land and naval forces, as well as advanced electronics, information technology solutions and customer support services.

<p>Operating group</p>	<p>Electronics, Intelligence & Support</p> 	<p>Land & Armaments</p> 
<p>Principal operations</p>	<p>Electronic Solutions Information Solutions Platform Solutions Support Solutions</p> <p>The Electronics, Intelligence & Support operating group designs, develops, produces and services systems and subsystems for a wide range of military and commercial applications. It comprises four lines of business: Electronic Solutions, Information Solutions, Platform Solutions and Support Solutions.</p>	<p>Global Combat Systems Global Tactical Systems Security & Survivability US Combat Systems</p> <p>The Land & Armaments operating group provides design, development, production, through-life support and upgrade of armoured combat vehicles, tactical wheeled vehicles, naval guns, missile launchers, artillery systems and munitions.</p>
<p>Main operating locations</p>		
<p>Major markets</p>	<p>US UK</p>	<p>US UK Sweden South Africa</p>
<p>Employees (including joint ventures)</p>	<p>33,900</p>	<p>21,300</p>

¹ Including share of equity accounted investments.

Programmes & Support	International	HQ & Other Businesses
		
<ul style="list-style-type: none"> BVT Surface Fleet Detica Integrated System Technologies Military Air Solutions Submarine Solutions 	<ul style="list-style-type: none"> Air Astana BAE Systems Australia CS&S International MBDA Saab 	<ul style="list-style-type: none"> BAE Systems plc BAE Systems, Inc. Chairman's Awards Commercial Company Giving Communications Education Partnerships Engineering Group Business Development Group Finance Group Legal Group Strategy HR Investor Relations Logistics & Information Systems Office of the Chief Executive - Corporate Responsibility - Internal Audit - Performance Excellence Procurement Project Management Regional Aircraft Shared Services Strategic Capability Solutions
<p>The Programmes & Support operating group comprises the company's UK-based air and naval activities, the activities of the acquired Detica security business and the Integrated System Technologies business.</p>	<p>The International operating group comprises the company's businesses in Saudi Arabia and Australia, together with a 37.5% interest in the pan-European MBDA joint venture, a 20.5% shareholding in Saab of Sweden and a 49% shareholding in Air Astana.</p>	
		
<p>UK</p>	<p>UK/Europe Middle East Australia</p>	<p>HQ & Other Businesses comprises the regional aircraft asset management and support activities, head office and UK shared services activity, including research centres and property management.</p>
<p>30,200</p>	<p>19,200</p>	<p>1,800</p>

Chief Executive's Statement

We continued to make good progress during 2008 in further embedding responsible business conduct and other areas of corporate responsibility (CR) throughout our business.

The focus of our Executive Committee is total performance against every aspect of the way we do business: not only financial and programme performance, but also business conduct and CR. It is vital that we achieve the same degree of rigour and pursuit of continuous improvement in CR as we do in our financial and programme management. We want to have an inclusive culture in which the talents and skills of every one of our employees are recognised and used.

Reflecting our commitment to be recognised as a leader in responsible business worldwide, we have updated the first of our Group Strategic Objectives to 'Continue to embed a high performance culture including delivery of our CR agenda' (see page 2).

In May 2008, the Woolf Committee, an independent body appointed by the Board under the chairmanship of Lord Woolf, to review the Company's ethical standards, published its report. A steering group and associated working groups have been established to address all 23 recommendations, and a plan has been developed for implementation of these recommendations within three years. The aim is to establish the Company as a leader in business conduct, not just within our sector but within the global business community.

Consistent with the importance attached to CR and the drive towards leadership in business conduct, we have taken steps to embed such issues more directly in our day to day operations. An important part of this drive is the establishment of a global Code of Conduct which gives all employees a clear understanding of what is expected of them. The global Code of Conduct was launched in January 2009 to codify the required standards of personal and business conduct.

In September 2008, we appointed Raj Rajagopal to the new post of Managing Director Corporate Responsibility, reporting directly to myself. As a particular focus, he will help to ensure that high standards of safety and ethical business conduct are a key element of executive performance and central to everything we do at BAE Systems. Raj leads a team that is developing and supporting implementation of our CR programme. This encompasses business conduct, safety, health, environment, diversity and inclusion, social and community issues, and reputational risk throughout the organisation.

Providing a safe working environment for all of our employees and all those who work on our sites is a key priority. We are determined to continually improve safety standards across our business to levels comparable with other leading global companies.

While we have demonstrated real improvements in safety, we were deeply saddened by the tragic loss of five of our employees. We are reviewing and addressing the causes of these incidents and are fully supporting these enquiries.

We are determined that we shall be recognised as a leader in responsible business worldwide and we continue to strive for ways to improve our business and its reputation.



Ian King
Chief Executive



Our Strategy

Our goal is to be the premier global defence, security and aerospace company. We have firmly embedded our corporate responsibility (CR) agenda as a strategic objective within our Company strategy.



Our Company strategy (see diagram) emphasises our commitment to total performance in every aspect of our business – not only financial and programme performance, but also business conduct and other parts of our CR agenda. Our new organisation structure reflects this commitment, with the Managing Director Corporate Responsibility reporting directly to our Chief Executive, who is ultimately accountable for CR. As part of our Operational Framework the Executive Committee is responsible for driving our CR agenda, and the Line Leaders are supported by the Managing Director Corporate Responsibility.





BAE Systems' CR agenda and activity has matured considerably since we began reporting in 2001. To achieve our objective to demonstrate leadership in responsible business worldwide will require a sustained and focused effort to embed the necessary behaviours and an inclusive culture across all of our businesses. A key part of this will be delivering on the recommendations contained in the Woolf Committee Report to ensure we are recognised as a global leader in standards of business conduct (see page 14).

Leadership and role model behaviour at the most senior level are key to helping us fulfil our strategy. Our 2008 objectives on ethics, safety, and diversity and inclusion were to demonstrate leadership, as well as making progress towards our stated goals. To confirm the importance of these objectives, 12% of the available executive bonus allocation was set against performance on safety and ethics objectives.

During 2008, significant progress was made against the ethics objectives including developing the global Code of Conduct and commencing the rollout to all employees from January 2009. We are also on plan with our programme to implement the Woolf Committee recommendations. The Remuneration Committee awarded the full stretch payout to the executive directors in respect of that part of the annual incentive related to ethics performance.

On safety, all major operational sites achieved Level 3 (other than those acquired during the year) against the five-level Safety Maturity

Matrix and have submitted plans to achieve Level 5 by end of 2011 (see page 16). Senior leaders undertook formal training and completed safety audits. The gap between Company performance and external benchmarks on days lost to work-related injuries was closed by just over 9% during the year, falling short of the target of 10%. The Remuneration Committee awarded only one-third of the potential payout on that part of the annual incentive determined by safety performance.

In 2009, 12% of the available senior executive bonus will continue to be determined by our business conduct and safety performance.

Inclusion objectives have also been set within the individual performance objectives for the senior leaders. We continue to develop other aspects of our CR agenda, in particular environment and sustainability.

Our CR Committee, chaired by non-executive director Andy Inglis, reviews progress against our objectives quarterly. The CR Committee provides independent oversight, advice and strategic direction on business conduct, social and environmental issues. In 2008, the Committee's activities included:

- Oversight of health and safety performance
- Review and oversight on the development of our global Code of Conduct
- Ongoing review of performance against objectives
- A site visit to our Submarine Solutions site in Barrow-in-Furness, UK, to review and understand how CR has been embedded within the business.

Identifying our material issues

In 2007, we identified the CR issues which we believed to be the most material (relevant and significant) for our business. We analysed the issues that could have an impact on the sustainability of BAE Systems, either by directly impacting the Company's ability to operate or by affecting our reputation and the level of trust which our stakeholders have in our Company.

Following this review process, the following two priorities were identified and a programme was put in place to address them:

- Ethics – achieving leadership performance through implementation of the Woolf Committee recommendations
- Safety – ensuring a consistent level of good safety management in the short term and driving safety performance to a level comparable with leading companies over a four-year period.

In 2008 and 2009 we set management objectives to help drive us towards our desired leadership position in the areas of ethics and safety.

Diversity and inclusion is also recognised as an increasingly important issue for our business. The sustainability of our workforce and our ability to win and fulfil global contracts depends on our ability to recruit and retain the most talented people from all backgrounds.

Our environmental performance is also of increasing importance both due to the nature of our operations and growing interest in this issue among stakeholders, including our customers.

Our objectives

2008 objectives	Progress	2009 objectives ²
Business Conduct		
Establish global leadership standards of business conduct:		
- Senior leadership to communicate and demonstrate commitment to high ethical standards through employee engagement. Number of engagement events and employees reached to be measured.	- Senior leadership used opportunities of team meetings and conferences to emphasise importance of ethical business conduct.	- Senior leadership to lead two employee focus/engagement sessions to discuss the global Code of Conduct and ethical issues.
- Develop and roll-out a Group-wide Code of Conduct.	- Roll-out of the global Code of Conduct to employees across the Group commenced in January 2009 (see page 13).	- Deliver the 2009 Woolf Committee implementation plan milestones and obtain independent external assurance of this.
- Implement the response to the Woolf Committee recommendations.	- Detailed programme in place to implement Woolf recommendations, with a number of actions already addressed (see page 14).	- Employee sample survey on selected ethics questions to be carried out in the fourth quarter of 2009. Results to show an improvement relative to the 2008 survey results.
Safety		
Continue to drive performance in safety to a level comparable with leading performers:		
- Days lost to work-related injuries: Reduce the gap between 2007 Group performance and external benchmark by 10% in 2008 (benchmark is 2,000 days lost per 100,000 employees).	- The gap between Group performance and the external benchmark was reduced by just over 9% during 2008.	- Senior leaders each to undertake three safety audits, and flow-down training and requirement to conduct safety reviews to two levels below the Executive Committee.
- Senior leadership to demonstrate commitment to safety by undertaking formal training and conducting safety audits across our operations. Number of safety audits conducted to be measured.	- Training sessions held between May and August. Safety audits conducted by senior leaders (see page 16).	- Minimum of Level 3 on the SMM, with 60% of sites progressed to Level 4 by the end of 2009.
- Progress to benchmark safety performance against a five-level Safety Maturity Matrix (SMM) – all businesses to achieve Level 3 by the end of 2008 and have a plan in place to attain Level 5 by the end of 2011 (Level 5 has been benchmarked against leading companies).	- All BAE Systems' major operational sites (other than those acquired during the year) achieved Level 3 by the end of 2008. All businesses submitted Level 5 plans by the end of 2008.	- Incident rate targets to be set by businesses at a level reflecting the progress required to achieve the 2011 target of best in class.
		- Incident rate in 2009 to show at least a 10% improvement over 2008 and, for sites with significantly worse than best in class statistics, improvement targets to be set consistent with achieving best in class in 2011.
Diversity and Inclusion		
Create an environment that values and respects the contribution, based on merit, of all members of the communities in which we operate:		
- Senior leadership to demonstrate commitment to such an environment by attending a diversity awareness training programme by mid-year.	- A workshop on the role of leadership in establishing a diverse and inclusive culture was held in June at a senior leaders' forum. Many of the attendees led similar events with their management teams.	- Senior leadership to participate in a workshop to develop the inclusion agenda for their business. Senior leaders to lead two events with employee groups to develop action plans to address culture, barriers and improvements.
- Establish a Group-wide Women's Forum.	- Inaugural virtual global Women's Forum was held in June with 70 participants across seven locations from three countries. Eighteen locations in three countries participated in the second forum in October.	- Executive Committee to review the Operational Framework and supporting policies and processes to identify potential improvements required to develop a more inclusive culture. Initial changes to be included in the updated July 2009 version of the Operational Framework.
- Develop an action plan to enhance diversity and inclusion by mid-year.	- Each business set an action plan to address specific diversity and inclusion issues identified in the Employee Opinion Survey. A summary of the 2008 survey results is set out on page 28.	- Senior leadership to develop one personal objective on inclusion during the first half of 2009 for implementation in the second half of the year.

² Business Conduct and Safety objectives are two of the Executive Committee's top ten objectives for 2009. Diversity and Inclusion objectives have been set within the individual performance objectives for the senior leadership.



Going Forward

In 2008, we created a new position, Managing Director Corporate Responsibility, to reinforce our commitment to achieving leadership performance in responsible business worldwide. Raj Rajagopal has been appointed to this position and reports directly to our Chief Executive, Ian King. As former President of our Ground Systems business, Raj has extensive knowledge of BAE Systems and a track record of successful programme management. His remit includes ensuring the Company's policies and processes meet with high standards of business conduct. He will also be responsible for developing and supporting the implementation of our policies on safety, health and the environment, and helping to embed them throughout the Company.

In 2009, our CR team will review our CR agenda and identify medium and long term goals. Their remit will be to:

- Establish a CR plan to support the Company's strategic direction and CR objectives. This will include metrics and Key Performance Indicators
- Ensure adequate resources are available to implement the CR Plan
- Support leaders in implementing our 2009 CR objectives
- Develop assurance criteria for Woolf implementation and CR Reporting for 2009
- Support the CR Committee
- Ensure effective, timely and accurate external reporting of the Company's CR activity.

Raj Rajagopal Managing Director
Corporate Responsibility

Stakeholder Engagement

Productive relationships with our stakeholders are essential to the effective running of our business and our ability to deliver high quality products and services.

Our stakeholders include employees, shareholders, trade unions, customers, business partners, suppliers, governments, CR specialists and local communities. We engage regularly with these groups to explain our approach and update them on changes in our business. We welcome feedback to help determine priorities and improve performance.

We also seek views and feedback on our CR programme from relevant specialists. These interactions improve confidence in our Company and help us move towards best practice.

Activity during 2008

Some of the ways that we have engaged stakeholders are included in the table on this page.

In addition, during 2007/08 the Woolf Committee met a large number of external stakeholders. These included representatives from government, investors, pressure groups and non-government organisations, peer companies and industry associations. Their views informed the Committee's final recommendations to BAE Systems. We are committed to continuing this dialogue with

interested external parties both helping us to shape required changes within BAE Systems, and agreeing broader defence industry approaches.

There are some key groups, in particular non-government organisations, with whom we recognise we need more proactive engagement going forward.

Responding to feedback

Last year, we asked a panel of experienced CR practitioners for their views on our CR strategy, governance and reporting. The table on page 7 shows how we have responded to their recommendations during 2008. A new commentary from the panel is included on page 8.

Activity during 2008

Employees

- Employee survey completed every two years, see page 28
- Global and local newsletters, team briefs and intranet sites
- Employee networks, including our Global Women's Forums and Networks
- 71 employee focus groups held to aid the development of our new global Code of Conduct.

Trade unions

- In the UK: we held 18 corporate level meetings with trade unions, including two Q&A sessions with our Chief Executive, quarterly corporate consultative meetings and monthly meetings with senior union representatives. We also consulted trade union working groups on a wide range of business issues including pensions, development of our Code of Conduct and review of the UK Respect at Work Policy
- In our US Combat Systems line of business: Management at five of our sites held regular meetings throughout the year with the six relevant unions. Unions are also involved in site safety committees and sometimes in employee training initiatives such as apprenticeship programmes
- In Sweden: Four unions attended eight meetings chaired by the business unit MD to discuss issues such as finance, market status and projects.

Shareholders

- Held 169 one-to-one meetings and 46 group meetings for investors to meet with senior management and our investor relations team
- Two site visits held, attended by five investor groups.

Customers

- Worked with the UK's Ministry of Defence to develop its Sustainable Procurement Charter, see page 23
- Supported the UK Government in efforts to develop an International Arms Trade Treaty.

Local communities

- Our businesses engage with communities on local issues. Examples include our Submarine Solutions business which runs a Local Liaison Group for community groups
- We engage with local communities globally through Company Giving and Charity Challenge initiatives
- Through our education programmes we encourage more young people to consider careers in science and engineering.

Business partners

- A founder and active member of the industry task force on anti-corruption and business of the Aerospace and Defence Industries Association of Europe (ASD)
- Continued to support the Defense Industry Initiative (DII) on Ethics and Business Conduct, to which BAE Systems Inc has been a signatory since 2002
- Supported dialogue between the ASD Council and Aerospace Industries Association in the US which aims to agree common industry standards on ethical business conduct.

Suppliers

- Worked with key suppliers through our supplier management and development programmes (see page 25) and in the UK our commitment to the Aerospace & Defence industry's 21st Century Supply Chains (SC21) improvement programme.

Governments

- Held regular meetings with government officials in our home markets to discuss public policy on defence and other business issues.

CR specialists

- The Woolf Committee recommendations are informing our approach to business conduct, see page 14
- Our CR Panel gave feedback on our strategy and reporting, see pages 7-9.

CR Panel – 2008 recommendations

Performance and plans

Strategy	
Develop a five-year plan for CR including targets and milestones.	During 2008 we reviewed our CR agenda and identified medium and long-term goals. During 2009 our new Managing Director Corporate Responsibility will develop a strategy for embedding CR across our businesses and regions, and a scorecard for monitoring progress.
Move from a CR strategy serving business needs to a business strategy conducted responsibly, and from compliance and risk avoidance to opportunity and value creation.	CR is now a key part of our Group strategic objectives (see page 2). Our newly appointed Managing Director Corporate Responsibility reports directly to the Chief Executive and will support this.
Communicate and embed the Company values more effectively.	During 2008 we increased our communication with managers and employees on CR. For example, this included regular items in Company Brief, monthly face-to-face briefings, and articles in BAE Systems News and on our intranet. Embedding an ethical culture is part of the work being undertaken following the Woolf Committee Report (see page 14). We launched our global Code of Conduct, which reinforces our ethical business principles, in January 2009. This covers our key CR issues including business conduct, safety, diversity and inclusion, and environment. The Code is being distributed to all employees through a briefing and cascade process and is being supported by an annual training programme.
Improve safety performance by an order of magnitude by focusing on culture, targets and leading (rather than lagging) indicators.	Senior managers are leading our efforts to embed a safety culture across BAE Systems and conducted a series of safety audits. During 2008, each of our businesses provided a rating against our Safety Maturity Matrix. All major operational sites (other than those acquired during the year) achieved our Level 3 target. 12% of the available bonus for senior executives was linked to performance on ethics and safety during 2008. Our safety performance improved in 2008 with the number of days lost to work-related injuries per 100,000 employees decreasing by 9% (See page 16).
Develop a global climate change policy. Improve environmental measurement and set ambitious targets.	We have calculated our carbon footprint and will use this to set emissions reduction targets to cut our impact on climate change. We have also signed the UK Ministry of Defence's Sustainable Procurement Charter. One element of the charter is an agreement to develop jointly sustainable measurement criteria, including climate change, and to implement processes and tools to enable the supply chain to work towards sustainable procurement and best practice (See page 23).
BAE Systems' human rights responsibilities need to be fully scoped, involving wide stakeholder participation.	We are developing our approach to a human rights policy for BAE Systems.
Governance	
Clarify how BAE Systems' committees and audit bodies relate to each other and provide assurance that they are fit for purpose.	Working group established to review board and management operations and define the role of our newly appointed Managing Director Corporate Responsibility (See page 5). We also held a joint meeting of CR and Audit committees in November 2008.
Clarify how senior responsibilities cascade to employees. Engage employees more effectively in performance improvement.	In 2008 senior managers carried out safety audits and training at our sites to raise awareness among employees. Performance on ethics and safety accounted for 12% of the available bonus for senior executives. A number of senior employees already have safety included in their personal scorecards. During 2009 we will look at ways we can extend business conduct and safety objectives to more employees.
Clarify the Company's processes for preventing bribery and corruption.	In 2008 we revised our policy on the appointment, management and payment of Business Development Advisers – which have been the source of some stakeholder concern about potential for corruption (see page 13). The revised process was described by the Woolf Committee as representing leading-edge practice. Our new global Code of Conduct (see page 13) aims to improve employee understanding of our approach and what it means to them. Our governance and external reporting on these issues will also be reviewed as part of our response to the Woolf Report recommendations.
Undertake a full stakeholder engagement process. Work towards setting up a broad-based Stakeholder Panel.	As part of the Woolf Implementation Plan a working group was established to review external engagement and map key stakeholder groups (see page 14–15). This group will consider the recommendation to set up a broad-base Stakeholder Panel.
Reporting	
Align reporting with Global Reporting Initiative guidelines.	Our current focus is to align our reporting with recognised standards over a three year period.
Set targets and report progress for all areas of current focus.	We report progress against our business conduct, safety, and diversity and inclusion targets described on page 4.
Provide more discussion on the legitimacy of the industry and more detail on products and services.	Our CR website is being revised to include more detail and background information. We will also improve links with other areas of the site, including product information.
Refocus reporting from shareholders to employees and other stakeholders.	An internal communications strategy was launched to increase employee awareness of our CR programme. We will continue to review reporting requirements.
Consider appropriate external audit and verification of reported information and data.	Deloitte were appointed to provide independent assurance on our 2008 Report using the ISAE 3000 standard.

For the second year BAE Systems charged the Panel with providing expert comment on our corporate responsibility (CR) strategy, governance and reporting and to offer advice on how to achieve leadership performance on our CR priorities.

Composition

- **Julia King**, Vice President Corporate Responsibility, *GlaxoSmithKline*
- **Dawn Rittenhouse**, Director of Sustainable Development, *DuPont*
- **Mark Wade**, *Context* affiliate, formerly Head of Sustainable Development Policy, Strategy & Reporting, *Shell* (Chairperson)

Brief

BAE Systems charged the Panel with providing expert independent comment on our CR strategy, governance and reporting and to offer advice on how to achieve leadership performance on our CR priorities.

The Panel met twice during the year, and reviewed material on our CR strategy and a draft of our 2008 CR Report. They were briefed by Deborah Allen, Deputy Managing Director Corporate Responsibility on BAE Systems' progress in 2008 and future ambitions.

The Panel was not asked to provide assurance or verification of systems or performance data.

Commentary

Strategy

BAE Systems has made a significant stride forward in seeing CR as central to the way it does business. This is evidenced by CR being embedded in the Group Strategic Objectives, the focus of the Executive Committee on total performance that includes CR, and the appointment of a senior CR Executive reporting directly to the Chief Executive.

In doing so, BAE Systems has responded wholeheartedly to the central tenet of the Panel's recommendations of 2008 to move from a CR strategy serving business needs to a business strategy conducted responsibly. This marks an important milestone on BAE Systems' drive to becoming a leader in business conduct not just in the sector but in the global business community.

The Panel acknowledges the progress made in identifying CR priorities and putting in place the necessary structures and resources for addressing them. The Panel encourages BAE Systems now to consolidate their thinking and commitments into a clear strategy for implementation across all aspects of the business. The Panel recommends this takes the form of a long term plan, including

milestones and targets, and BAE Systems makes this public. Such a move will be a powerful driver for change within the organisation and a signal of determination for all to see.

The Panel is pleased that a key recommendation to communicate and embed company values has been taken to heart. This is evidenced by the development of the new principles-based global Code of Conduct embracing what is expected of every employee with regards to CR including business conduct, safety, diversity and inclusion, and the environment.

The Panel notes that efforts on ethics awareness and behaviour have already led to a 7% increase in staff stating they believe BAE Systems demonstrates ethical standards.

BAE Systems' commitment to engaging all staff and developing training on the Code is welcomed. The Panel recommends that this also be central to employee induction.

The unequivocal commitment by BAE Systems to act on all 23 recommendations of the Woolf Report and the setting up of the necessary structures for implementation is applauded. 2009 will be a test of the Company's resolve in moving from intent to delivery.

The Panel recognises the determination of senior leaders to drive safety improvement. This is evidenced by their personal involvement in safety audits and the reduction in their bonuses because of the failure to meet the target of a 10% reduction in days lost to work-related injuries.

The Panel applauds the ambition to embed a 'culture of zero tolerance of unsafe working.' This recognises that engendering the right mindset is as important as setting the rules. The Panel recommends that these elements be central tenets of all safety training and that ultimately BAE Systems commits to a goal of zero injuries to send the clear message that all injuries can be prevented.

The use of the Safety Maturity Matrix is seen as a sound basis for driving continuous improvement in a structured and auditable way. It is recommended that the construct of the matrix and its elements be better explained in future Reports and/or through a web reference.

It is further recommended that the definitions used for collating and reporting data be made consistent with industry standards to aid meaningful comparison.

The Panel notes that it is insufficient just to report the identification of the causes of injuries. It is necessary for the organisation to develop a fundamental understanding of the

underlying reasons for injuries and to make clear the actions that will be taken to prevent reoccurrence. This should be addressed in future reports.

In spite of the failure to meet the 10% reduction target, achieving just over a 9% reduction in days lost due to work-related injuries in 2008 is creditable. BAE Systems is urged to build on progress, define clear targets and milestones across the safety agenda, and move from lagging to leading indicators as recommended last year.

The calculation of BAE Systems' global carbon footprint is a major first step to developing a climate change strategy and setting emissions reduction targets. It is recommended that the footprint data be examined at a detailed level across all aspects of operations to drive down costs and impacts.

It is recommended that a set of environmental Key Performance Indicators and targets be defined for other key environmental parameters.

The Panel applauds BAE Systems signing the UK Ministry of Defence Sustainable Procurement Charter. This shows industry leadership and a determination to carry best practice into the supply chain.

The Panel notes the start made in defining what human rights means for BAE Systems and early work on diversity and inclusion. The Panel recommends that BAE Systems seeks input from human rights organisations to enrich thinking and better understand societal expectations.

The Panel applauds the efforts BAE Systems is making to understand the potential issues associated with its products and the early steps being taken to address them. The Panel encourages BAE Systems to take a full lifecycle approach with a view to going beyond compliance.

Governance

The Panel is impressed with the systematic way in which BAE Systems has established a governance structure and clear senior executive accountabilities for CR and its elements. This includes the appointment of a Managing Director for CR and a comprehensive set of working groups for the implementation of the Woolf Committee recommendations and other CR priority areas.

It remains the recommendation of the Panel that BAE Systems show in this Report the accountabilities and inter-relationships of the various governance structures. This will provide clarity and the necessary reassurance to staff and other parties that they are integrated and fit for purpose.

It is encouraging to note the innovation occurring in the ways the business divisions engage with staff on CR, safety recognition and reward systems, and the use of the Ethics Helpline. It is recommended that emerging best practice be exchanged and consolidated into new standards of working.

BAE Systems is urged to seek wide expert stakeholder input to policy development across the CR agenda and in particular to human rights and climate change.

Reporting

Independent assurance helps to add rigour to management processes and builds trust in processes and behaviour. The Panel is pleased to see the strides taken in providing assurance on the CR Report compilation to the ISAE 3000 standard. The aim to align reporting to recognise standards over a three year period is welcomed. The Panel continues to recommend that BAE Systems works toward aligning reporting with Global Reporting Initiative guidelines.

The Panel is pleased that a communications package based on this report will be produced for staff. The Panel recommends that the contents of the report also be used as the basis for wider stakeholder engagement through the web and other means.

The Panel is encouraged by the first signs in this report of BAE Systems' willingness to provide real insights into the nature of its products and services, their use and the people who make and support them in the field.

The Panel encourages BAE Systems to go further and to engage wholeheartedly in the debate on the legitimacy of the industry, BAE Systems' role within it and the associated issues and impacts. BAE Systems' statement that it does not produce land mines and cluster bombs is a powerful start.

The Panel recommends that BAE Systems systematically identifies and addresses the key issues it faces using stakeholder input. Such issues should include the use of Business Development Advisers, offset agreements, end user certificates, lifecycle impacts and product composition and disposal.

The Panel encourages BAE Systems to build on its impressive first steps and be bold in addressing the issues it confronts in a transparent and engaging manner. Only by doing so can BAE Systems' CR aspirations be fully credible.

Mark Wade

Context

"BAE Systems has made an impressive stride forward in seeing CR as central to business strategy. The challenge now is to embed this throughout the organisation in a systematic manner and unleash the value creation potential."

Julia King

GlaxoSmithKline

"BAE Systems needs to confront and report the issues it faces in an engaging and transparent way. Only then will its aspiration for responsible business conduct be fully credible."

Dawn Rittenhouse

DuPont

"It is insufficient just to report the identification of the causes of injuries. It is necessary for the organisation to develop a fundamental understanding of the underlying reasons for injuries and to make clear the actions that will be taken to prevent reoccurrence."



Business Conduct

We are determined to be recognised as a leader in responsible business conduct worldwide, and we continue to strive for ways to improve our business and its reputation.

Maintaining high standards of business conduct is essential to enhance our overall business performance, build trust, and maintain and improve our reputation with stakeholders. Our licence to operate depends on this.

Strong principles

Strong principles and standards are the cornerstones of business conduct. Our global Code of Conduct is a summary of the principles and standards of business conduct expected of all our employees wherever they operate. All employees are required to comply with the standards set out within the global Code of Conduct.

Our ethical business conduct principles

Accountability: we are all personally answerable for our conduct and actions

Honesty: there is no substitute for the truth

Integrity: we say what we will do, we do what we say

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

Respect: we value each individual and treat them with dignity, respect and thoughtfulness.

Embedding a total performance culture

We want to be recognised as a high performing company not only in terms of our financial and programme performance, but also as a leader in all aspects of business conduct.

Visible leadership

Our senior leaders are expected to promote a collective and individual sense of responsibility for business conduct, and are committed to lead by example. This includes conducting regular briefings emphasising the importance of business conduct and discussing issues with employees. Senior leaders are supporting the rollout of the global Code of Conduct and training to employees (see page 13).

Continuous improvement in business conduct is included in the objectives for all Executive Committee members and linked to their remuneration (see page 4).

Ongoing Investigations

The Company is subject to the continuing investigation by the UK Serious Fraud Office (SFO) into suspected false accounting and corruption, which was originally announced in 2004. The Company is co-operating fully with the SFO.

In June 2007, the Company was notified by the US Department of Justice that it had commenced an investigation relating to the Group's compliance with anti-corruption laws, including its business concerning the Kingdom of Saudi Arabia.



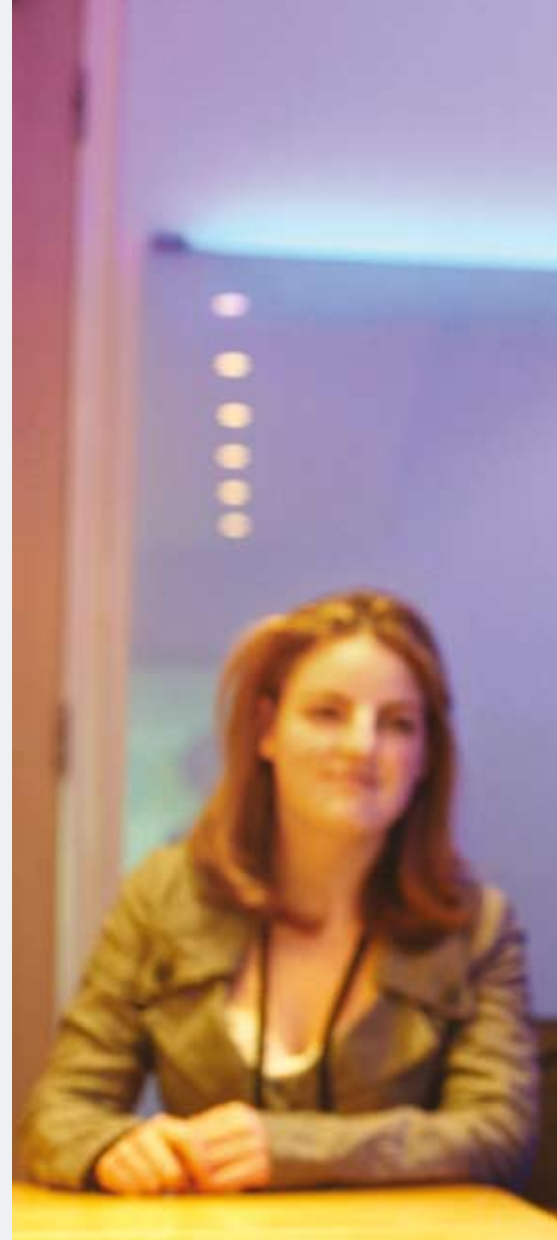
Bob Fitch

Head of Government Relations in the US

"Business conduct is one of many factors that define a world class company. I've worked at BAE Systems and its legacy companies since 1993 and know this is of key importance to our employees and customers.

Embedding an ethical culture means making this relevant to employees in all our home markets. We must ensure that employees are fully engaged in the process. Face-to-face briefings by our leaders will have a big impact.

Communicating our approach externally is also very important. As Head of Government Relations in the US, I am responsible for establishing and maintaining relationships between our Company's leaders and senior officials in the executive and legislative branches of government. With the new administration in the US and our position as a growing defence company, we need to make sure people know not just who we are but what we stand for as a company."







Types of call to Ethics Helpline³

Resulting in enquiries ■ UK/RoW ■ US

Accounting charges practices	2	82	International business issues	0	2	Contract compliance	0	3
Company ethical practices	5	0	Procurement, trade and marketing	1	11	Management practices	11	69
Conflicts of interest	2	102	Quality or manufacturing issues	0	4	Environmental, Health and Safety	0	10
Employee relations and conduct	35	122	Security and misuse of assets	2	20	Guidance and advice	24	0
						Total	82	425

³ Enquiries include both requests for information and allegations of misconduct whether substantiated or not.

Global Code of Conduct

Our new global Code of Conduct brings together working practices already in place in various parts of the business. The Company has had a series of policies and principles for some time and in some parts of the business these were reflected in local codes. The new global Code of Conduct was launched in January 2009 and provides BAE Systems employees with a common document containing the principles and standards expected of all employees, regardless of location or role.

Practical examples are included to provide general guidance on situations that may arise in employees' day to day activities on behalf of the Company. It encourages employees to ask for help and emphasises that they can raise concerns without fear of reprisal.

The Code has been benchmarked against global companies by the Ethical Leadership Group (an independent consultancy) and the Institute of Business Ethics. We held focus groups with employees and managers in all of



our home markets to review the draft Code of Conduct and gained trade union feedback by holding two dedicated UK trade union focus groups. In total, 71 focus groups were held involving over 700 people.

The Code is being rolled out to all employees from 2009 through face-to-face briefings. The aim is full engagement with all employees. Every employee will be asked to confirm that they have understood and will comply with the principles and standards in the Code. The roll-out of the Code will be supported by mandatory training. On completion of the training we expect employees to be able to:

- Understand the principles in the Code
- Explain why all employees must take responsibility and be accountable for their own actions
- Recognise when to ask for help and take appropriate action.

The rollout of our global Code of Conduct supports the implementation of our strategy. The full Code of Conduct is on our website at <http://www.baesystems.com/AboutUs/OurGlobalCodeofConduct>

Ethics helpline

Our Ethics Helpline exists so that employees can report ethical concerns from our business, confidentially, wherever they operate and whatever their role.

Clear policies

Key business policies and processes are mandated across the Company by our Operational Framework, which sets out the way we do business and what it means to be part of our Company. It is based on principles of good governance, a set of definitions, values, policies and processes that guide our work and behaviour, and a clear system of delegated authority.

Following the work on our global Code of Conduct, two new policies have been introduced. We published our new Environment Policy in January 2009 (see page 20). The new Lobbying and Political Support Policy provides additional focus and definition of the Company's position. The standard, as defined in our Code of Conduct, states we will not make political payments. We will be open about our lobbying activity.

We will continue to review and refresh our policies and processes on a regular basis as part of our commitment to continuous improvement.

Business Development Advisers

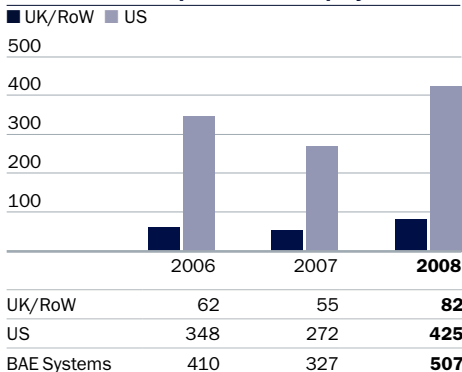
The use of advisers is common in many industries. They provide essential knowledge of local markets, rules and organisations.

Some stakeholders are concerned that the use of advisers may be associated with corruption.

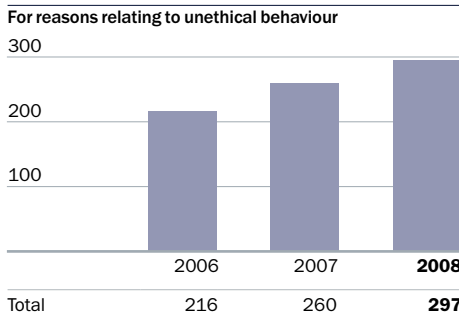
In 2007, we undertook an extensive programme to revise our policies, processes and procedures with regard to the appointment, management and payment of Business Development Advisers. Central to this process is the creation of a Business Development Adviser Compliance Panel. The Panel is chaired by independent third parties. The revised process was described by the Woolf Committee as representing leading-edge practice.

During 2007 and 2008, whilst the new process for the appointment, management and payment of advisers was being designed and implemented, the Company also undertook a review of current contracts with existing Business Development Advisers and of expired contracts with outstanding obligations; this exercise included a review of these arrangements by the Panel. As a result of the review, and the Company's stated strategy to focus on the development of home markets, many

Formal ethics enquiries from employees³



Dismissals



Business Development Adviser contracts were either terminated or expired without renewal. As defined in the revised process, decisions by the Company to re-appoint, or maintain the contract and services of a Business Development Adviser are subject to the Company receiving from the Panel prior affirmative advice to do so. As a result of the actions described above, the number of Business Development Advisers has been substantially reduced.

Implementing the Woolf Committee recommendations

The Woolf Committee Report was published in May 2008. It made 23 recommendations for further improvement. These provide a route map for the Company to establish a global reputation for high standards of business conduct. The Committee's full report is available on our website at www.baesystems.com/woolfcommittee

We have committed to act on all the Report's recommendations and have put in place a comprehensive implementation programme of up to three years to achieve this. In order for us to deliver this programme successfully, the outputs of the implementation programme must quickly become part of how the Company conducts its day-to-day business as a key part of its performance culture.

The Executive Committee has appointed the Group General Counsel as sponsor of a programme to implement the Woolf Committee findings and reinforce high standards of business conduct as a sustainable way of working across the Company. The programme, which is led by a full-time Programme Director and a central team of 14 people, applies project management disciplines and processes to the programme similar to those applied to the Company's projects. A Steering Committee, drawn from

members of the Executive Committee and other senior leaders, has been established to provide strategic oversight to the programme and to monitor progress regularly.

As part of the Implementation Programme, the Programme Team has divided each of the 23 recommendations into six key areas of operational activity, with each area being addressed by a Working Group. These six Working Groups consist of approximately 60 senior managers drawn from across the global BAE Systems business. External professional advisers have also been engaged to support the focus of the Programme. The scope of work being carried out in the Working Groups is as follows:

(i) Customer Contracting – developing procedures to assess the ethical and reputational risks involved with the selling of defence equipment and capability by BAE Systems. Such assessments are planned to form part of our consideration of what equipment and capabilities we sell, to whom we sell it, and what contractual obligations we will accept.

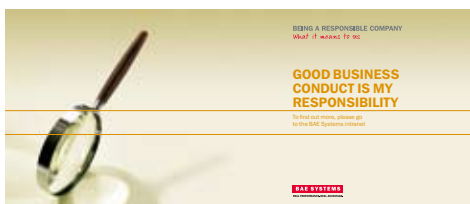
(ii) Anti-Corruption and Compliance – assessing and recommending changes to our anti-corruption policies, procedures and guidelines. This work includes codifying and integrating the existing policies on Business Development Adviser appointments, and recommending further enhancements to anti-bribery policies and procedures. Other policies under review include those relating to facilitation payments, gifts, hospitality and donations, Company giving, sponsorship, conflicts of interest together with internal investigations and disciplinary policy concerning breaches of business conduct policies.

(iii) Board and Management Operations – recommending enhancements to corporate governance arrangements with respect to the management of non-financial risk. This Working Group was responsible for recommending the establishment of a new role of Managing Director Corporate Responsibility as well as developing procedures to embed further the explicit consideration of ethical and reputational risk in the Company's decision-making.

(iv) Leadership in business conduct – defining and articulating the strategic aspiration and intent of the Company to be a leader in standards of business conduct among global companies. This Working Group is also defining the role and performance management assessment (including remuneration) of BAE Systems' senior executives, the development of a business conduct and compliance training strategy, and the drive for openness and transparency.

(v) External engagement – recommending actions to support the Company's leadership in the defence industry on key matters of ethical and reputational risk. This covers a wide range of external stakeholders such as governments, non-governmental organisations, customers and competitors.

(vi) Establishing a global Code of Conduct – focusing on the delivery and implementation of a new global Code of Conduct to communicate the required principles of business conduct and the standards expected of all employees, regardless of location or role, consistent with the Company's aspiration and intention to be a leader in standards of business conduct among global companies.



Above: Posters used to communicate launch of the Code of Conduct to employees

Looking forward

The global Code of Conduct is at a very advanced stage and the first phase of the work for the Working Groups is nearing completion. This phase involves identification of the actions necessary to implement each of the recommendations in the Woolf Committee Report, exploring options for change and proposing solutions. The status of these proposed solutions was reviewed, in detail, by the Steering Committee in December 2008.

The next planned phase, to be undertaken in the first half of 2009, is a consultation process both inside and outside the Company on these proposed solutions. We plan that the feedback from this consultation will be fully considered in formulating the final design of the changes to be implemented.

The programme to implement the recommendations of the Woolf Committee is an extensive and thorough undertaking of up to three years during which changes will be progressively implemented across the Company. As stated above, we already have a revised policy relating to the engagement of Business Development Advisers. In addition, we have reinforced our training in standards of business conduct and have taken initial steps to include a greater emphasis on assessing non-financial risk in the assessment of customer bid proposals.

Once we have fully implemented the necessary changes, our intention is that BAE Systems will be recognised as a global leader in standards of business conduct.

Our progress in implementing each recommendation will be monitored regularly by our Corporate Responsibility Committee. Independent external auditors, Deloitte, have been appointed to assure our progress annually.

The Woolf Committee – key facts

What was it?

An external, independent committee appointed by the BAE Systems Board in 2007.

Why was it convened?

The Committee's remit was to study and report publicly on our ethics policies and processes and make recommendations aimed at achieving a leadership position in ethical business practice among corporate industry peers. Its recommendations were published in May 2008.

Members

- The Rt. Hon. The Lord Woolf of Barnes (Chairman), former Lord Chief Justice of England and Wales
 - Sir David Walker, Senior Adviser and former Chairman of Morgan Stanley International Ltd
 - Philippa Foster Back OBE, Director of the Institute of Business Ethics
 - Douglas N Daft AC, former Chairman and Chief Executive of The Coca-Cola Company
 - Dr Richard Jarvis (Secretary to the Committee), former Secretary to the Committee on Standards in Public Life.
-



Dick Olver

Chairman, BAE Systems

"The Woolf Implementation Programme is of fundamental importance to how we do business now and in the future, and it will derive benefits for our employees, customers, and shareholders. We believe the Woolf Report provides valuable insight and observations that BAE Systems, the defence industry, and all global companies can learn from."

Health, Safety and Environment

We have a collective responsibility to maintain a healthy and secure workplace and to promote safe working practices. As a global company we must also use resources efficiently and minimise waste.

Health and Safety

We firmly believe that ensuring the safety of our employees and those who work on our sites is a pre-condition of our operations. We recognise the risks associated both with manufacturing and daily office work, and seek to ensure that these risks are managed and mitigated as far as is reasonably possible. In 2007, we declared our aspiration and commitment to achieving a level of safety comparable with the best in class. This section provides an update on our progress towards this goal.

Many of our employees are involved in manufacturing, often using heavy equipment and sometimes handling explosive or nuclear materials. In addition, a number of BAE Systems employees are based at customer sites providing maintenance and support services. These include military bases in combat zones, such as Iraq and Afghanistan.

Our goal is to achieve a leadership level of safety performance, compared with the best performing companies worldwide. This requires a significant reduction in workplace accidents and injuries. Our target, based on the performance of leading companies, is to be below 2,000 days lost to work-related injuries per 100,000 employees. Our performance in 2007 was 10,084⁴ days and in 2008 this was reduced to 9,336 days. We reduced the gap by just over 9% in 2008, below our 10% target.

In 2007, we launched a four-year plan with safety targets for every BAE Systems business. We are focusing on sharing best practice and embedding a safety culture across the Group. We are also working closely with our customers to ensure the safety of employees based off-site where we do not have operational control.

A clear safety strategy

Our goal is to ensure a consistent level of good safety management in the short term and drive safety performance to a level comparable with leading performers over a four-year period.

We developed a five-level Safety Maturity Matrix (SMM) to help us progress towards recognised best practice and continue to improve performance across our sites. Our target is for all our businesses to achieve Level 5 (benchmark) by the end of 2011.

In 2008, each business provided a rating against the SMM. Initial ratings ranged from Levels 1 to 4 and plans were set in place to achieve Level 3 across all BAE Systems businesses by the end of 2008. This was achieved across all BAE Systems' major operational sites (other than those acquired during the year). Further benefit was gained from our safety professionals supporting audits of other sites across our operations. This delivered cross-site learning, improved networking and exchange of good practice.

We recognise that 'best in class' is a continually improving target and we will annually review the criteria we are aiming for. This will be supplemented by ongoing benchmark visits with other companies to understand how we can keep raising our standards of safety.

Continuous improvement in safety performance is included in the objectives for all senior executives and linked to their remuneration (see page 4).

Embedding a safety culture

We must embed a safety culture where there is zero tolerance of unsafe working practices and unsafe working conditions. Visible leadership and effective employee engagement is essential.

Visible leadership

Senior leaders demonstrated their commitment to safety by undertaking formal training and personally conducting site safety audits in 2008. This initiative was designed to inspire employees and give senior managers an insight into safety issues affecting employees on the shop floor.

We plan to make safety audits led by senior managers a regular feature of our approach to safety management. In 2009, we will involve the next two levels of management from across BAE Systems.

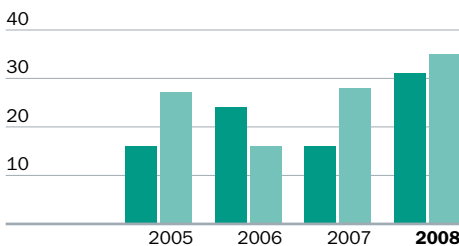
Employee awareness

New employees receive a safety briefing as part of their induction and all employees receive ongoing briefings and training specific to their roles and responsibilities. Employees must take responsibility for their own safety and that of others with whom they work with.

We are focusing on raising employee awareness of safety at a local level. For example, our Submarine Solutions business at Barrow, UK, produced a DVD for employee briefings with the message, 'I could have saved a life today ... but I looked the other way'. It reinforces the message that everyone has a responsibility to report unsafe practices, regardless of whether they are directly involved and even if they feel awkward about discussing it. All employees at our Submarine Solutions business are required to watch the DVD.

Employees and subcontractors working at our Ship Repair business in San Diego and Norfolk in the US, are awarded tokens when observed either engaging in safe work practices or preventing unsafe acts. Tokens can be redeemed for BAE Systems merchandise, and employees awarded six or more tokens in a six month period receive a cash award of US\$100.

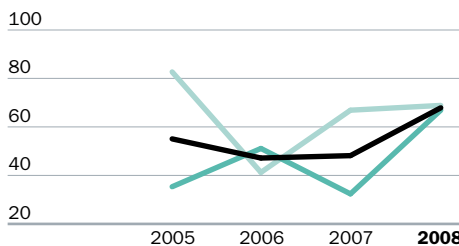
Major injuries recorded



■ UK/RoW	16	24	16	31
■ US	27	16	28	35
Total	43	40	44	66

Major injuries recorded

Rate per 100,000 employees



■ UK/RoW	35	51	32	67
■ US	83	41	67	69
■ BAE Systems	55	47	48	68

UK manufacturing average 2007/08: 181

⁴ We previously stated the 2007 figure as 8,734. This has been revised following a thorough review of baseline information.

⁵ In 2008, the main causes of major injuries continue to be slips, trips or falls on same level. These continue to be addressed across our business.



Addressing safety challenges in Saudi Arabia

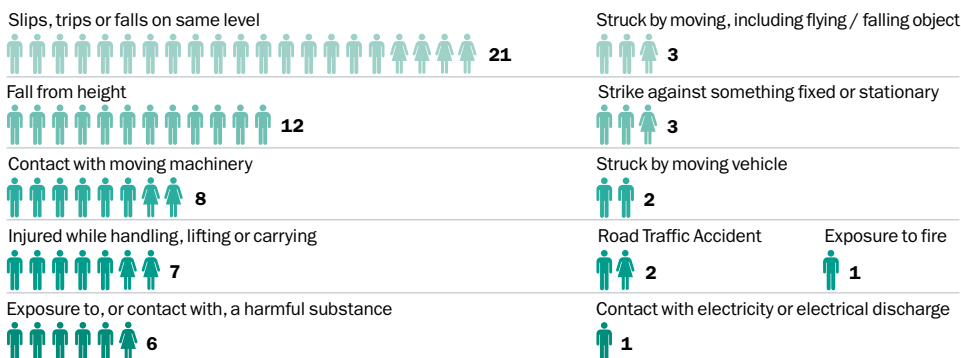
Military Air Solutions (MAS) has been actively involved in lending a helping hand to Customer, Solutions & Support International (CS&SI) colleagues in Saudi Arabia. The support began in the summer with a whistle-stop tour of sites in Saudi Arabia to understand the challenges the business is facing, and to begin development of a support plan.

The plan, agreed in September, sees a rolling programme of MAS SHE professionals seconded to Saudi Arabia to provide assistance to CS&SI SHE personnel in delivering key elements of the Safety Maturity Matrix. The initial tour was a success and helped pave the way for investment in existing infrastructure to eliminate SHE issues.

It is not all one-way, though, as the Saudi experience is seen as an opportunity both to share best practice between the businesses and to broaden international experience for MAS employees.

2008 Cause of major injuries recorded⁵

Number of employees injured



Improving employee health

We have a number of programmes to help employees take care of their health and reduce time away from work. Examples include:

South Africa – HIV/AIDS Awareness

HIV/AIDS is a serious problem in South Africa and many of those affected do not have access to treatment. Infection rates are even higher among the working population. This has serious implications for any company operating in South Africa.

Land Systems South Africa has implemented an awareness and treatment programme. Employees receive information and training on HIV/AIDS to help them understand the causes and treatment options. Free and confidential testing is provided to encourage employees to find out their HIV status. The business works hard to create an environment where employees trust that testing is confidential and are encouraged to come forward.

The business now understands the level of infection within its workforce (but not the names of individuals personally affected) and can plan accordingly. All employees who test positive are given access to free health care, anti-retroviral treatment and counselling. This is provided through a third party organisation to ensure employee confidentiality.

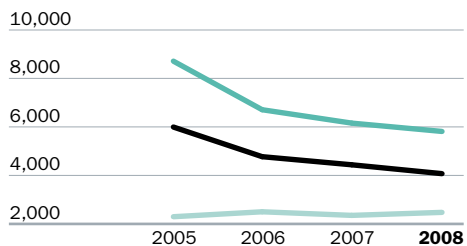
Health management at US Combat Systems

Our US Combat Systems business offers a number of programmes to help employees improve their health. Programmes include disease management and case management support for employees and their spouses with chronic conditions, health assessments, wellness seminars and disease prevention programmes. Web and phone-based support helps employees lose weight, quit smoking, and deal with depression and alcohol abuse. The business provides free flu vaccinations, a fitness programme and enables employees to order fresh fruits and vegetables to be delivered to the work place. The Fridley site follows a modified catering menu which offers lower calorie options for meetings held on-site.



Total recorded injuries to all employees⁶

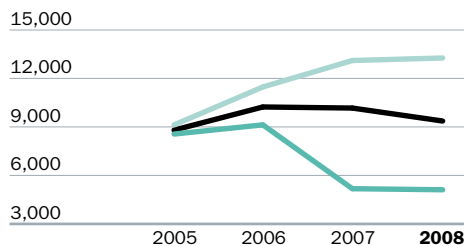
Rate per 100,000 employees



■ UK/RoW	8,723	6,722	6,171	5,828
■ US	2,315	2,518	2,370	2,494
■ BAE Systems	6,009	4,788	4,454	4,089

Days recorded lost to work-related injuries⁷

Rate per 100,000 employees



■ UK/RoW	8,530	9,099	5,152	5,086
■ US	9,096	11,441	13,077	13,233
■ BAE Systems	8,774	10,204	10,084 ⁸	9,336

⁶ In 2008 the total injury rate (per 100,000 employees) decreased by just over 8% from the previous year, but the rate of major injuries went up by 41%. This increase is primarily related to the expansion of the Australian business, via acquisition and improvements in data reporting.

⁷ The days lost to work-related injuries per 100,000 employees have decreased by just over 9% from the previous year to 9,336. While this shows improvement, we have not met our target to reduce the gap between our performance and an external benchmark of other companies by 10% during 2008. The benchmark is 2,000 days lost per 100,000 employees.

⁸ We previously stated the 2007 figure as 8,734. This has been revised following a thorough review of baseline information.

⁹ For reporting purposes, fatalities are included within the year that the incident occurred.



Sharing best practice

Leadership safety performance requires a consistent approach across our different sites and businesses. The exchange of ideas, policies and best practice is essential.

Safety professionals from our businesses in the UK and US conducted audits of our sites against our Safety Maturity Matrix during 2008. During the audits, the experts shared best practice with other BAE Systems' businesses and learned from examples of excellence in different sites and regions.

We also partner with customers on safety where we have employees based off-site at customer locations. For example, our Military Air Systems (MAS) business in the UK jointly developed a Safety, Health and Environmental (SHE) Management System with the UK Royal Air Force to help ensure effective SHE Standards across RAF bases where BAE Systems employees work. The initiative was launched by BAE Systems to ensure legal compliance, but this collaborative working enabled the achievement of ISO 14001 and OHSAS 18001 for all MAS activities at customer locations.

Fatalities

We are saddened to report the deaths of five employees⁹ in 2008. These include two fatalities at our sites – one during a crane operation at our shipyards in San Diego, US, and one during a maintenance procedure at our aircraft facility in Brough, UK. We are reviewing the causes of these accidents and co-operating fully with regulatory investigations. Our shipyard in San Diego has made a number of management changes as a result and our Brough site is implementing a 15-point remedial action plan.

Three fatalities occurred among our employees deployed with the US armed forces in Iraq and Afghanistan, as part of the Human Terrain System (see page 27). These are subject to ongoing military procedures and investigation. We recognise the bravery of these individuals in being prepared to enter dangerous territories to support the work of our armed forces.



Mike Gee

UK Head of SHE Assurance

"If we want to be a leading defence, security and aerospace company, that means not just being good engineers, innovators and people managers but we need to deliver world class safety too.

Since recently returning to work at BAE Systems after a number of years in other industries, I have noticed a step change in safety management. Our new Safety Maturity Matrix (SMM) provides a common process for measuring and managing SHE performance across the business. This is particularly important now that we operate in so

many different countries around the world. We also have the opportunity through the SMM process to leverage the wealth of experience that exists within our organisation through the sharing of best practice worldwide.

Embedding a safety culture is a never-ending task. If we become complacent, we won't succeed. Senior leaders have made a great start at demonstrating their commitment by personally taking part in safety reviews. We need to extend this and encourage all employees, business partners and contractors to play an active role."

Environment

We recognise that our day-to-day operations, our products and their use and disposal have the potential to damage the environment. To keep our impact to a minimum, we must manage our resources efficiently and minimise waste. We also need to consider the lifecycle of our products including how they are maintained and disposed of.

Reducing the environmental impacts of our operations helps us to cut costs, improve efficiency and comply with the growing volume of environmental regulation. Concerns around climate change and rising energy costs mean that our environmental performance is of growing interest to all of our stakeholders.

This section explains how we are tackling the environmental footprint of our operations, including our manufacturing sites and offices. Product environmental impacts are covered in Product Stewardship (page 22).

Our Environment Policy

We published our new Environment Policy in January 2009. This states our commitment to reducing resource use, minimising the environmental impacts of our products throughout their lifecycle and establishing environmental performance targets. It is included in our global Code of Conduct that is being distributed to all employees (see page 13).

We work in partnership with customers and suppliers on environmental issues. In 2008, we were the first signatory to the UK Ministry of Defence's (MOD) Sustainable Procurement Charter (see page 23).

Climate change

Our primary contribution to climate change comes from CO₂ emissions associated with the energy we use for heating and lighting and the travel footprint of our employees. In 2008, we commissioned the Coefficient Company to provide an analysis of our total carbon footprint for 2007 to give us a view of our global emissions.

Their analysis took into account not just emissions from electricity use, but also from coal, oil, aviation fuel used to test our aircraft and business travel. On this basis, our total carbon footprint was estimated at around 920,000 tonnes of CO₂ emissions in 2007. We reported in 2007 that 550,000 tonnes related to energy use (business travel not included within the reported figure). The analysis also identified areas where data was not being correctly reported by individual sites.

In 2007, 79% of our total emissions related to the use of electricity and natural gas at our sites (see chart). Another 15% of our emissions were as a result of business travel. Around 89% of our total emissions are from our operations in the UK and US (see chart).

Our businesses are looking into initiatives that could help reduce our carbon footprint by implementing energy saving measures and sharing best practice. We are also looking for ways to reduce business travel.

In 2009, we plan to extend our data collection to include CO₂ emissions from product trials. We have developed new technologies that will help our customers reduce emissions, such as HybriDrive™ technology used for both military and civilian transport (see page 24). We are also working with the UK MOD to calculate the carbon footprint of the lifecycle of defence equipment.

Eight of our sites participate in the EU Emissions trading scheme. In 2008, we transferred or traded 13,750 tonnes of carbon.

We report our greenhouse gas emissions to the Carbon Disclosure Project, a collaboration of institutional investors on the business implications of climate change.

Initiatives to reduce our impacts

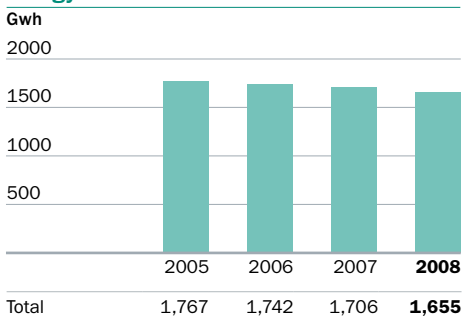
Energy use

In 2007, electricity use accounted for 60% of our footprint. We encourage our sites to implement energy saving measures and help them to share best practice through initiatives such as our Major Energy User Group.

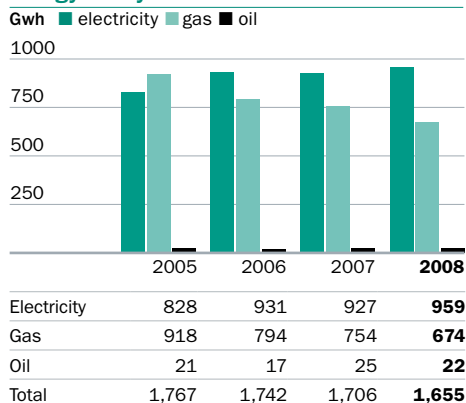
Recent examples include:

- Submarine Solutions have appointed 80 employee Energy Monitors in the UK to identify energy waste and encourage colleagues to save energy. The site has installed translucent roof panels, double glazing of windows and efficient lighting schemes to reduce electricity consumption
- Our Australian business has introduced a number of energy saving initiatives that include using eco-friendly IT servers that consume 40% less energy, installing low wattage lighting across major sites and installing solar power technology to refurbished buildings
- Continuous improvements have taken place across our Swedish business with a number of initiatives introduced to control temperature more efficiently and reduce the amount of energy used in lightning. For example, lighting in offices is controlled by sensors and shuts down if there is no movement in the room
- During 2008 Electronics, Intelligence & Support in the US continued the roll out of its Utility Cost Takeout (UCT) approach across its major sites. UCT requires sites to carry out

Energy use¹⁰



Energy use by source¹⁰



CO₂ emissions relating to energy use¹¹





Norfolk Ship Repair's award winning environmental programme

BAE Systems Norfolk Ship Repair has saved more than £9 million since 2000 by cutting waste and supporting local ecosystems.

In 2008, 8 million pounds of paper, wood and scrap metals were sold for recycling, yielding more than £172,330 in revenues and significantly reducing the amount of waste sent to landfill. Around 93% of hazardous waste was sold to a facility for use as fuel in cement kilns.

An on-site water treatment plant enables more than 30 million litres of industrial wastewater to be purified instead of being sent off-site for disposal. This saved more than £896,119 annually benefiting the Company and its customers. An additional 5.7 million litres of water were saved by recovering steam condensate for reuse in boilers.

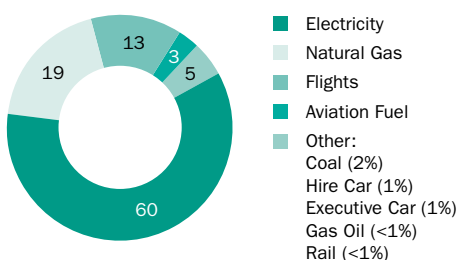
The site is now home to two acres of wildlife friendly habitats. Employee volunteers have planted thousands of wetland plants and trees to support these, which include an 8,000 square feet oyster reef, two inter-tidal wetland areas and osprey nest stands.

The Norfolk Ship Repair site has won more than 12 environmental awards since 2000, including an Environmental Excellence Award from the Virginia Governor in 2008. The site was recently nominated for a US Environmental Protection Agency award for environmental achievements.

Norfolk Ship Repair's environmental team is sharing best practice across BAE Systems and has also worked with local waterfront businesses to help them improve their environmental performance.

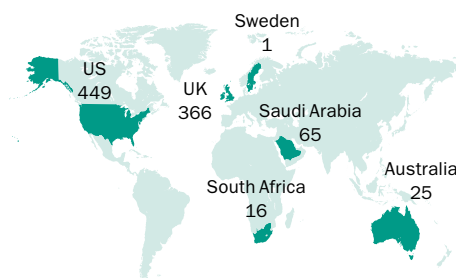
2007 CO₂ emissions by source¹²

Percentage



2007 CO₂ emissions by market¹²

Thousand tonnes CO₂



¹⁰ In 2008, we reduced our total energy use by 3% from the previous year. The reduction has been achieved as part of ongoing energy initiatives across our business globally.

¹¹ Total carbon emissions are reported as 0.66 million tonnes. This year we have adopted Defra's guidelines on Greenhouse Gas Conversion Factors for Company Reporting 2008.

¹² Based on analysis by the Coefficient Company for our 2007 carbon footprint.

an audit of all buildings and external facilities to review utility usage and how it can be made more efficient. Energy saving initiatives introduced following the audit include the installation of a closed loop cooling system to reduce water use and the introduction of sensor-driven lighting to cut energy use.

Business travel

In 2007, business travel accounted for 15% of our footprint, mostly from flights. During 2008, our businesses looked for ways to reduce business travel.

For example, our Insyte business has been trialling new video conferencing technology to reduce employee travel and allow people in different locations to work together more effectively. The system uses High Definition display with improved video and sound quality. A series of lunchtime demonstration sessions have been held to give employees first-hand experience of the new facilities and other remote meeting technologies.

Waste and recycling

Our operations generate both hazardous and non-hazardous waste. The wide variety of national legislation on hazardous waste and materials is a challenge. To meet this challenge, our Land & Armaments business is developing its own list of materials which it considers unacceptable and plans to eliminate from its products. This list – to be published in 2009 – will be more stringent than the requirements of some countries where we operate.

Our Submarine Solutions business designs, integrates and commissions nuclear powered submarines. Elements of these activities pose a potential hazard to the workforce, the public and the environment. Consequently these activities are subject to strict legislation and

regulations including the Nuclear Installations Act, Ionising Radiation Regulations, Radioactive Substances Act and the Health and Safety at Work Act. Any activities which could impact the safety of the workforce, general public or environment are also subject to Regulation by the Nuclear Installations Inspectorate (NII), the Ministry of Defence (MOD) (through the Defence Nuclear Safety Regulator (DNSR)) and the Environment Agency (EA). Process teams are responsible for ensuring that appropriate Nuclear Safety management arrangements and processes are in place.

Other impacts

There were 29 reportable environmental incidents, which included spillages, leaks and discharges, at our sites in 2008. Action plans have been put in place to address these areas.

Product stewardship

The nature of our products makes it essential that they can be depended upon and used safely. This includes use, handling and transportation.

Our customers are also interested in the environmental performance of our products. For example, concerns around climate change and rising energy costs are making product energy efficiency an increasingly important issue.

We take a lifecycle approach to product stewardship – seeking to minimise potential risks to operators, the public, property and the environment from design to manufacture and supply, use and disposal.

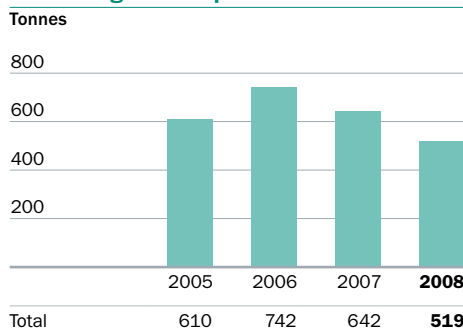
Improving product safety

We publish Product Environmental Guidance to help our employees and engineers analyse a product's potential environmental impacts and take steps to reduce these throughout the lifecycle. Work to develop environmental courses was started in 2008 and these will become part of our general training and development for engineers.

Our Product Environmental Working Group (PEWG) supports the identification and sharing of best practice, and facilitates the incorporation of environmental considerations into our design, maintenance and disposal processes in the UK. The Group, established in 2007, will be working more closely with our sites in Australia and North America.

Our business operating groups are required to define, implement and maintain a Product Safety Management System which specifies roles and responsibilities – including an independent governance role. In addition it details processes which include those for the

Volatile organic compound emissions¹³



¹³ We achieved just over 19% overall reduction in Volatile Organic Compounds from 2007 to 2008, while production increased in a number of areas across operations.

safety assessment of our products, training requirements for those engaged in safety related design activities, auditing, the review of user training, handbooks and other support/usage documentation.

In a role that mirrors the PEWG, our Product Safety Working Group (PSWG) supports the identification and sharing of best practice. To date, this has predominantly been within our UK business but we have made progress during 2008 in improving links across our global operations. In the US, for example, both operating groups have now established a Community of Practice (CoP) for Product Safety practitioners and experts, with links to the UK PSWG.

In the UK, the PSWG runs one-day conferences twice a year. In 2008 these focused on the role of suppliers, and product safety during maintenance and support. Around 70 employees participated in each session. Speakers shared their experience and best practice from the various businesses across BAE Systems, and learned from external domain experts.

In 2009 we will set up a similar working group in the US, supported by both product safety and product environmental practitioners in each line of business.

Senior managers are responsible for implementing the Product Safety Management System in each business. As part of our Operational Framework, managers are required to confirm compliance twice a year.

Our products in the field

High quality, technical and accurate systems and weapons contribute to the safety of the troops using them and reduces the risk of civilian injury.

We do not manufacture land mines or cluster bombs.



Air conditioning protects soldiers on the battlefield

For soldiers in Iraq, temperatures on the battlefield can reach approximately 54°C outside and more than 65°C inside a Bradley Fighting Vehicle. This level of heat can seriously affect their health, lower morale and hinder military operations.

BAE Systems and the US Army have developed a heat abatement system for the Bradley to lower temperatures, provide a safer environment and increase soldiers' combat readiness. Since the system was first introduced in August 2008, the BAE Systems team in Baghdad has installed the system in 104 vehicles by the end of the year, with another 500 vehicles to be upgraded by June 2009. The heat abatement system reduces the ambient temperature for the squad by up to 23°C, and individual chiller vests provide regulated cooling to the driver, commander and gunner.

Soldiers using the modified vehicles have told us what a difference air conditioning makes to their lives.

Working with the UK Ministry of Defence (MOD)

In 2008, we became the first major supplier to sign the MOD Sustainable Procurement Charter. This commits the MOD and its biggest suppliers to work together to achieve sustainable development goals through educating suppliers, developing performance measures and sharing best practice. We will ask our own suppliers to sign the Charter and work with them to implement environmental improvements.

We work with the MOD on a range of other environmental initiatives. One example is the Green Commander Fleet Radar Programme which is incorporating eco-design principles in radar development.

We have also developed a model for understanding the advantages and disadvantages of different energy options. This will help the MOD assess energy needs, identify reduction opportunities and assess the costs and environmental benefits of different energy sources.

We monitor our Corporate Responsibility performance through sector benchmarking to track our performance and help us better manage key environmental and social impacts. In 2008, our performance level in the Dow Jones Sustainability World Index was 70%, 3% lower than our 2007 score.

We are reviewing the reasons for the lower environmental factors rating in 2008, which include the areas of environmental reporting, product impact and management systems. We will address areas for improvement during 2009.

Dow Jones Sustainability World Index

	2006	2007	2008
Economic factors	69%	69%	68%
Environmental factors	85%	90%	74%
Social factors	80%	71%	70%



Hybrid buses reduce city emissions

BAE Systems' HybriDrive™ technology is helping public transport agencies in North America reduce their environmental impacts. More than 2,500 hybrid buses, which run on a mix of diesel and electric power, are currently in use in Houston, New York, Ottawa, San Francisco, and Toronto. They are also on trial in the UK and Japan.

HybriDrive™ buses increase fuel economy by approximately 30%, whilst reducing emissions and offering a smoother ride. To date, these buses have collectively travelled more than 70 million miles, saved nearly 18.9 million litres of diesel, and prevented more than approximately 45,000 tonnes of carbon emissions.

Hybrid electric drive systems were initially developed for vehicles in our military portfolio.

Supporting renewable energy

We are supporting technology development in the renewable energy sector by applying our engineering expertise to develop new improved wind turbines and prevent wind farms interfering with radar systems.

Working together with our naval joint venture BVT Surface Fleet, we are supporting the UK Energy Technologies Institute's deepwater turbine project. Our role will include helping to design high-voltage offshore wind turbines that will be able to function, on either a mount or a floating base, in depths from 30 to 300 metres.

The number of potential sites for new wind farms is significantly reduced because wind turbines can interfere with aircraft and maritime radar, and radio. We are working with the UK government and Vesta, a wind technology company, to find a solution to this problem.

Radar absorbing materials, traditionally used to prevent radar detection of military aircraft and ships, can be used within wind turbine blades to prevent them interfering with nearby air traffic control and national security radar systems. We are also developing an Advanced Digital Tracker, a filter that can be added to new and existing radar systems, blocking out wind farm interference. This technology will enable wider use of wind energy.

Many of our products are designed to increase the safety of armed forces in combat. These include military helmets, bullet-proof vests and armoured vehicles.

In 2008, BAE Systems received recognition at the 6th Annual US Army 'Top Ten Greatest Inventions Awards'. Our winning products included the Objective Gunner Protection Kit which increases protection for troops against explosive device fragmentation and enemy small arms fire.

Addressing environmental impacts

Our products have the potential to damage the environment during manufacturing, use, maintenance and disposal. Key impacts include:

- Emissions from vehicles and aircraft which contribute to climate change and affect local air quality
- Ordnance left over from wars or military training that can potentially contaminate land and water courses, and affect the health of local communities
- Disposal of hazardous materials from ships, aircraft and other military vehicles.

A number of workshops were held in 2008 to help employees understand the implications of new legislation such as REACH (Registration, Evaluation, Authorisation, and Restriction of Chemical Substances), RoHS (Restriction of the Use of certain Hazardous Substances in Electrical and Electronic Equipment Regulations) and WEEE (Waste Electrical and Electronic Equipment Regulations).

We are increasingly providing customers with a through-life service – maintaining and upgrading equipment during use, and disposing of products at end of life. This approach is expected to have environmental benefits. For example, it can enable customers to use the same hardware for longer, reducing raw material use and environmental impacts from manufacturing.

Reducing hazardous materials

Where possible, we are eliminating hazardous substances such as asbestos, lead, radioactive materials, and ozone-depleting chemicals from our products.

For example, our Land & Armaments business is eliminating or reducing use of hazardous materials in the design of its Future Combat Systems vehicles. Recent successes have included:

- Elimination of hexavalent chromium in chemical conversion coatings and anodise, and as a constituent in sealants
- Elimination of lead in bushings and bearings and use of lead-free solid film lubricants
- Elimination of cadmium plating
- Use of fire extinguishing agents which do not deplete the ozone layer
- Use of paints with lower levels of volatile organic compounds and no hazardous air pollutants.

We recently reviewed our compliance with the EU REACH regulations. Relevant substances manufactured or imported in quantities greater than one tonne per year have been pre-registered in accordance with the regulations. Further work is ongoing to ensure compliance with the regulations as a producer of articles and a downstream user.

Product CO₂ emissions

The climate impact of aviation has become a high profile topic as public concern about climate change increases. Our Regional Aircraft business is involved in a number of projects to reduce aircraft emissions. These include:

- Conducting an environmental impact study to assess the climate impact of our aircraft during manufacturing and use. The study identified several new technologies that may help to reduce fuel consumption and emissions such as lighter-weight composite materials and algae-based biofuels

- Publishing guidance to help operators of the BAe 146 and Avro RJ aircraft reduce fuel use and cut CO₂ emissions by up to 600 tonnes a year – by reducing unnecessary cabin weight, for example
- Participated in the first phase of the Single European Sky Air Traffic Management Research project which aims to improve the efficiency of European air traffic control, helping to reduce fuel use and CO₂ emissions.

We are investing in research and development of renewable energy technologies and increasing our product portfolio in this area. The case studies on Hybrid technologies and wind farms profile two recent examples.

Suppliers

BAE Systems spends over £9 billion a year on goods and services, with a supply base of more than 16,000 suppliers. Our reputation and the quality of our products can be affected by the suppliers with whom we do business. It is important that our suppliers provide high quality products and services, act ethically, treat their employees fairly, maintain high health and safety standards, and manage their impact on the environment.

The Company will require our suppliers to operate in accordance with an appropriate set of ethical standards equivalent to our own and will reflect this in our contracts with them. We will also continue to work with them to improve standards for the defence industry.

We share best practice with key suppliers through our Strategic Supplier Management programmes. Our most important suppliers are assessed regularly and we set targets to help them improve performance on a range of issues, including safety and product stewardship.

Hannah Sesay

Director Safety, Health & Environment, Land & Armaments

“Reducing the use of hazardous materials not only helps the environment, it makes good business sense. Customers want greener products.

As the director of safety, health and environmental, my role is to ensure common and consistent standards across the Land & Armaments (L&A) operating group for assessing risk and reviewing the environmental impacts of projects. With the right technology and knowledge, we can make a significant impact by working towards the elimination and use of hazardous materials in our products during the design phase.

With a global organisation such as L&A, the biggest challenge can be maneuvering around the different regulatory requirements and local definitions as to what is considered hazardous waste or material. That's why we are developing a list of materials that we consider unacceptable and will work towards eliminating those materials from our products.”



Our workplace is changing. A growing number of our employees are based at customer sites, providing maintenance and support services on military bases and for troops on the front line.

Our changing workplace requires new skills and capabilities and a different approach to people management. At the same time our business is expanding internationally as we increase our presence in key markets. We need to create a mobile workforce and use skills and capabilities from across BAE Systems to service customers wherever they are based.

These changes are taking place against the backdrop of a skills shortage and increased competition for science and engineering graduates in many of our home markets.

We must anticipate and respond to these trends. Our approach includes:

- Expanding our recruitment pool to include talented people from both genders and all backgrounds
- Creating an inclusive work environment that supports the retention of skilled employees, and encourages collaboration between employees in different markets
- Providing training to help employees keep abreast of changing customer requirements
- Good communication that keeps all employees involved and motivated regardless of location.

Diversity and inclusion

We aim to establish a diverse workforce. The main challenges are increasing the percentage of women in our workforce, and increasing ethnic diversity in countries such as the UK.

Our senior leaders are responsible for creating an inclusive work environment. This is included in the objectives for all Executive Committee members (see page 4).

Senior leaders received inclusion awareness training in 2008 to help them understand their role in creating an inclusive culture. This training outlined the business case for a diverse workforce and provided material to help leaders engage employees on diversity.

Our global Code of Conduct (see page 13) covers inclusive workplace behaviour. This is distributed across our businesses and encourages employees to report inappropriate or unacceptable behaviour, either by speaking to their manager or contacting our Ethics Helpline.

Gender

Increasing gender diversity continues to be challenging in our industry. Today, the percentage of female engineering and technology graduates remains low in many countries – only 15% in the UK, for example (according to Higher Education Statistics Agency data from 2005 to 2007).

Our approach to increasing gender diversity includes:

- **Education** – our schools programme challenges perceptions that engineering is a male career choice (see page 30).
- **Recruitment** – we have reviewed our graduate recruitment brochures and websites to ensure they appeal to a diverse audience and include case studies of female graduates
- **Leadership development** – we have identified female employees in each business who have the potential to become senior leaders. They have been appointed a senior mentor to help identify development needs and provide guidance on career planning
- **Flexible working** – many of our businesses enable flexible working, including part-time working
- **Women's networks** – these provide female employees with a wider network of contacts and support. They also act as a source of expertise to help the business identify barriers and enablers to the inclusion of women at all levels of the Company. In 2008 we held two women's forums, uniting more than 70 employees from a number of sites globally, to raise awareness of women's networks. These were led by senior

executives. We have also launched a 'Women at BAE Systems' online forum and held awareness sessions on women's networks across the business.

BAE Systems was included in the UK Times newspaper's Top 50 places Where Women Want to Work list in 2008, for the third year. In the US, BAE Systems was selected from over 500 nominations as Best Employer to Work For by the Institute of Electrical and Electronics Engineers' (IEEE) Women in Engineering magazine.

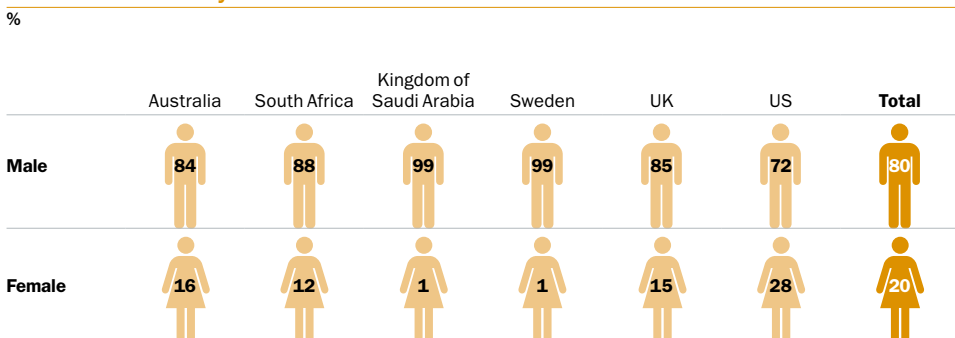
In 2008, the percentage of women in the business remained almost constant at 20% (compared with 21% the previous year).

Ethnicity

Our approach to ethnic diversity is tailored to local culture and heritage in each of our home markets, subject to compliance with local laws. For example, in South Africa we are increasing the number of previously disadvantaged individuals in the workforce, in line with the South African Government's Broad Based Black Economic Empowerment (BBBEE) initiative. In Saudi Arabia we are focusing on increasing the proportion of Saudi nationals in the workforce (see case study page 29).

In the US we are focusing on encouraging African American students to consider a career at BAE Systems. In 2008 we participated in the two-day career fair at the 2008 National Black Engineer of the Year Awards. We also sponsored a National Society of Black Engineers' Dinner, attended by high school students hoping to receive scientific, technical, engineering, or mathematical scholarships.

2008 Gender diversity





Supporting on the front line

The Human Terrain System (HTS) is a US Army programme which allows anthropologists to work alongside other social scientists with combat brigades (currently in Iraq and Afghanistan) to help tacticians in the field understand local cultures using Human Terrain Mapping. The goal of the HTS is to give commanders insight into the population and its culture in order to enhance operational effectiveness, and reduce military and civilian conflict.

BAE Systems Technology Solutions and Services (TSS) is the prime contractor on the HTS providing commanders in the field with relevant socio-cultural understanding to help meet their operational requirements. Our employees advise US Army units on economic development, political systems and tribal structures, and conduct research on topics of interest to the unit staff. BAE Systems also assists in the hiring process and strategic communications surrounding HTS work.

As of February 2009, there were approximately 450 BAE Systems TSS and subcontracted employees working to support HTS. Increased understanding of local cultures and socio-political realities has led to a significant decrease in violence.

In 2008, three fatalities occurred among our employees deployed on active service with the US armed forces in Iraq and Afghanistan, as part of the Human Terrain System. These are subject to ongoing military procedures and investigation. We recognise the bravery of these individuals in being prepared to enter dangerous territories to support the work of our armed forces.

Photo courtesy of US Department of Defense

Rosalind Murray

Winner of engineer of the year 2008, Operations Change Manager, Submarine Solutions

"I studied Materials Science and Metallurgy at University. After graduation I joined an accountancy firm, which I didn't enjoy at all so I came back to engineering and started in Barrow as a graduate engineer.

In my current role I'm helping bring lean manufacturing principles to submarine building. This involves coaching colleagues to improve the way they work. We have to show people that they have the power to change things – that's when improvements happen. I love the challenge and the knowledge I'm contributing to such an impressive and complex product. In the long term I'd like to be a company director, but we'll see what the future brings and I'll take it one step at a time.

In some ways being a woman in an engineering company can be an advantage, as it helps you stand out from the crowd. But it also brings quite a few challenges. It can be tough gaining credibility when working in what at times can be a macho culture. More often than not you are the only woman in the room and that can be quite intimidating.

We need to encourage more women to enter the industry. This means working with schools and universities and creating the right environment so that women feel valued and have the opportunity to build their careers. There are still lots of assumptions about the challenges that face

women in our industry. Making an effort to understand these is important to changing mindsets, even if it means asking uncomfortable questions.

I have been helping to set up and run the Submarine Solutions women's network. It's a great chance to share what I've learnt with others as well as learn from them. It has been fantastic to see the level of engagement within Submarine Solutions, and that the Company is taking the 'gender agenda' seriously."

Age

The average age of our workforce is an issue and we have succession planning in place to prepare the Company for changes as employees retire. Business initiatives include identifying high-potential employees and ensuring they work closely with those who are about to retire to transfer knowledge and expertise. Retirees are encouraged to share their knowledge through documentation and coaching sessions. Where practical, we offer flexible working for employees who would like to reduce their hours as they approach retirement and want to explore other activities.

Training and development

We must ensure that employees develop their skills and keep up with changing technology and customer requirements. In addition we support apprenticeships and other initiatives that increase the numbers of qualified engineers, technicians and project managers.

In 2008, we employed 347 new apprentices in the UK, and 712 people joined BAE Systems through our graduate recruitment programmes in the UK and the US. In addition, we employed 410 summer interns in the US, and 31 students in industrial placements in the UK.

We work with customers to develop and implement training for the defence industry. Skilling Australia's Defence Industry (SADI) is one example, sharing the responsibility for skills growth and development between the defence industry and the Australian government. Through the partnership we have helped launch the Military Systems Integration (MSI) programme, which is managed by the University of South Australia as a postgraduate course. It provides targeted training in a realistic environment using industry processes and procedures.

Employee development

Progress and development are monitored for all employees through annual performance and development review meetings. We have a leadership development scheme for high potential employees.

Our leadership programmes include:

- Assessment centres in the US which target potential senior leaders and candidates for Vice-President and President roles. Participants are assessed on their leadership competencies and style, and are provided with development planning support and coaching
- The Emerging Leaders Programme which is a new global programme focusing on identifying, selecting and developing high-potential employees. In 2008, 45 participants from around the world took part and all came together at a single event for the first time.

Employee communications

Good communication helps keep our workforce engaged and motivated. Our approach includes regular employee surveys, global, regional and departmental newsletters and our new global intranet site. We also engage with our people through employee representative bodies and trade unions. These relationships are important in helping us resolve issues and improve our employment policies.

This year, our biennial employee survey was completed by more than 58,000 employees. The survey helps us measure progress on implementing our CR objectives and responses showed strong awareness of our three CR priorities: safety, business conduct and diversity. Key results from the 2008 survey are shown in the table below.

In response to the survey results, the Executive Committee has agreed four performance improvement priorities for all parts of our business.

These are to ensure that:

- Personal performance objectives are clear and measurable
- People are properly recognised for doing a good job
- Business changes that affect us are communicated in a timely manner
- Our working culture enables everyone to demonstrate high standards of business conduct and to speak up and challenge inappropriate behaviour.

Each of our businesses has developed action plans to address local survey results, which will include measures to address the four global priority areas. The Executive Committee will regularly review progress made against action plans.

2008 Age diversity

%

25 years and younger



26-35 years



36-49 years



50-59 years



60 years and older



2008 Ethnic diversity

% in UK, US & South Africa

	UK	US	SA	Total
White	97	75	48	85
Non-white	3	25	52	15

2008 Ethnic diversity

% in Kingdom of Saudi Arabia

Saudi national	57
White European	33
Asian	0
Other	10

Key results from the biennial employee survey

%

Question	Favourable score in 2008	Change from 2006 score
Overall job satisfaction	71	+3
Satisfaction with career	56	+4
Belief that BAE Systems demonstrates clear ethical standards	73	+7
Clear and measurable personal objectives	67	-3
Receive regular updates on performance against the business plan and strategy	58	-3
Acting on Customer feedback	70	-3



Saudisation

In Saudi Arabia we are committed to training local nationals for management, technical and other qualified positions. This process is known as Saudisation. It brings social and economic benefits to Saudi Arabia and ensures that BAE Systems has access to a wider pool of talented employees.

The company focuses on supporting the career aspirations of its local workforce. Among our programmes is the Mustakbal management development scheme providing participants with career development support, leadership training and qualifications. Various long and medium term schemes are also used to equip employees with advanced engineering, technical and administrative skills.

Training is provided to customers and others in Saudi Arabia on a third party basis. We are involved in Royal Saudi Air Force (RSAF) training programmes, and have contributed to the training of 2,600 pilots and aircrew, 3,000 ground-based officers, and nearly 20,000 technicians over the past 33 years. Training related to Typhoon aircraft, industrialisation and for the Royal Saudi Naval Force has also been conducted.

Our programmes are having an impact. In 1994, we employed 700 Saudi nationals – 15% of our workforce in the country. Today, Saudis constitute 57% of the total number of our employees, making BAE Systems one of the country's largest private sector employers of Saudis. In 2007, the management board of Customer Solutions and Support International relocated from the UK to Riyadh, reflecting our commitment to developing our Saudi business. There is now Saudi representation on this board.



Debbie Sallis

Vice President Human Resources, Land & Armaments

“Our vision to be the premier global defence, security and aerospace partner is both exciting and challenging. It means our people need to deliver leading performance in very different environments; whether that be at a BAE Systems facility or working alongside our industrial partners and customers on their sites.

It helps to have people who understand local customs and languages but it is even more essential to respect different cultures and be open to working with a broad spectrum of colleagues. Our ability to work together across national boundaries will enable customers to tap into our immense capability anywhere in the world.

The challenge is finding competent individuals who are adaptable and willing to be a part of a diverse and often virtual team. Experience of living and working in another culture is an asset, particularly for key management and leadership positions. As more of our employees are stationed at customer facilities, some in conflict zones, we must ensure access to BAE Systems tools, support and advice. Thought and planning is required to help us select the right people for these roles, and ensure they are sufficiently adaptable and resilient to cope with varied – and often tough – working environments.”

Education and Community

We give time and money to support education and charities in our key markets. This is an important investment for our business. We invest in skills and will continue to do so.

Education programmes

Our education programmes are designed to interest young people in science and engineering and help combat the skills shortage affecting our industry. They challenge perceptions that engineering is a male career choice and support our efforts to recruit a diverse workforce.

Below are some examples of the numerous education programmes we supported during 2008:

- **Australia:** The Northern Advanced Manufacturing Industry Group (NAMIG) is a collaboration between BAE Systems Australia and other businesses to improve education for students in Northern Adelaide, an area of traditionally high unemployment and lower education standards. It aims to encourage more students to pursue careers in science, mathematics and technology through teacher and student industry tours, short courses, workshops and curriculum development
- **Kingdom of Saudi Arabia:** Provision was made for 20 Saudi academics to conduct research at UK universities in the summer through a programme organised by the British Council and supported by BAE Systems. The programme provides access to facilities, resources, papers and colleagues that would be otherwise unavailable to them
- **South Africa:** Our funding supported a maths teacher at a local school in Johannesburg and provided bursaries for talented students
- **Sweden:** Our employees in Örnköldsvik support schools and encourage interest in engineering by organising activities to help 7-14 year olds with their technical studies and two week practical training placements for older children

- **UK:** Our innovative schools roadshow reached over 15,000 young people, helping to challenge stereotypes about engineering and excite young people about possible careers in science and engineering
- **US:** Our employees volunteered at local schools helping elementary and high school children with their maths, science, reading and engineering studies. The programme is helping more students complete their studies and improve their grades.

Supporting charities

Our businesses support local charities through corporate donations and employee fundraising and volunteering. This helps us develop good relationships with the communities near our sites and motivate and engage our employees.

Our current partner charities are: Sue Ryder Care (UK), supporting people with serious illnesses; Leukaemia Foundation (Australia), supporting patients with leukaemia; America Supports You (US), helping members of the armed forces and veterans. BAE Systems gives £50 for every employee who spends a day volunteering for our partner charities.

Activities in 2008 included:

- 40 BAE Systems Australia employees volunteered 200 hours, to make the Leukaemia Foundation's 'Light the Night' event a success
- A team from Farnborough, UK, volunteered to help paint and decorate a local Sue Ryder Care Hospice
- Employees from CS&S International in Saudi Arabia raised approximately £15,000 for the Disabled Children's Association in a 'dash-for-cash' event. The five employees ran 254 miles, the distance from Riyadh to Dhahran, on a running machine in just 23 hours

- Electronics, Intelligence & Support employees donated 112 bicycles and helmets to the children of military families stationed at Fort Dix, McGuire Air Force Base and Lakehurst Naval Center. More than 30 employees helped assemble the bicycles on build-a-bike day.

Help for veterans and their families

Our support for troops and veterans in 2008 included:

- **Australia:** funding for the Australian War Memorial Trust
- **UK:** sponsorship of the Ministry of Defence's 'Christmas Box' scheme and morale-boosting concerts for troops organised by the British Forces Foundation. We made charitable donations to support wounded service personnel and to help provide accommodation allowing families and loved ones to visit UK rehabilitation centres
- **US:** support for United Service Organizations, a not-for-profit organisation which provides assistance to US military personnel and their families.

Monica Ingelsson

Education coordinator, Sweden

"I work with schools and colleagues within BAE Systems to enable students to visit our sites and find out about the different types of work we do. It is really exciting for children to see what we are doing with their own eyes, and can be very inspiring for them.

Older children can come to our factory for work experience for a week or more in the school holidays. We give them a half day session at each different station within the factory so by the end of the week they have seen the whole production line and all the different job possibilities.

This provides a great learning opportunity for the children. And it is really important to BAE Systems that there will be technically skilled people available to hire in the future. I also go out to schools to talk about what we do at BAE Systems and get the children interested in technical and engineering careers."



Investing in the workforce of the future

Since the early 1990s, BAE Systems has sponsored *FIRST* (For Inspiration and Recognition of Science and Technology), a non-profit educational organisation which strives to excite young people about science, technology and engineering through a robotic competition in the US. In 2008 we became a strategic partner with a contribution of more than £600,000 made in money, resources, and volunteer support, making us *FIRST*'s largest corporate supporter.

FIRST's goal is to create a world where science and technology are celebrated and where young people dream of becoming science and technology heroes. The annual *FIRST* Robotics Competition involves students from around the world. Teams of young people designed and developed a robot and competed in local competitions culminating in a two-day championship held in Atlanta, Georgia. More than 1,300 teams took part in 2008, increasing their skills and self-confidence.

BAE Systems supported some 70 teams from schools near our sites, several of which won awards for gracious professionalism, innovation, design and safety. We also sponsored 7 regional events and the *FIRST* championship. Employees from across our US business volunteered their time to mentor teams, judge competitions and support regional events.

BAE Systems also funds grants and college scholarships for *FIRST* students attending select universities across the US, with the goal of inspiring young people to choose careers in science and engineering.

As a result of our long standing commitment to *FIRST*, BAE Systems was awarded the 2008 Founders Award from Dean Kamen, inventor and founder of *FIRST*.

Supporting teachers in the UK

In 2008, BAE Systems agreed to be one of six corporate partners, each contributing £1m over 5 years, to Project Enthuse in the UK. Project Enthuse has been set up to help improve the quality of science teaching in schools across the country. BAE Systems funding and that of the other corporate partners, will ensure that over 2000 science teachers a year will be able to receive training on best practice in science teaching at the new National Science Learning Centre at York University. The aim of this project, is to see improvements in the attitude and motivation of young people to study science, which will hopefully increase the number of students studying A Level science.



Louise Routledge

Charity Challenge coordinator, Australia

“As a Charity Challenge coordinator, I help organise all the fundraising events at the Tamworth Flight Training site to benefit our charity partners. Doing something to help those less fortunate than myself is really important to me, and being involved in Charity Challenge gives me a great sense of satisfaction. It is also a fantastic opportunity to get to know colleagues working at other sites. There is a real sense of camaraderie and working together for a common cause.”

Assurance Statement

Independent assurance report by Deloitte LLP to BAE Systems plc on the Corporate Responsibility Report 2008.

What we looked at: scope of our work

BAE Systems plc ('BAE Systems') has engaged us to give assurance on:

Limited Assurance:

- their description, on the contents page in the section 'Report process', for compiling the Group CR report ('Group CR report compilation').

Reasonable assurance:

- their statement on the implementation of the Woolf Committee recommendations on pages 13-15 of their CR Report 2008, limited to statements made in the grey boxes under the headings Global Code of Conduct, Ethics helpline, Clear policies, Business Development Advisers, Implementing the Woolf Committee recommendations, Looking forward and the Woolf Committee – key facts.

What standards we used: basis of our work and level of assurance

Our work was carried out by a multi-disciplinary team of CR assurance specialists in accordance with the International Standard on Assurance Engagements 3000 (ISAE 3000).

For the CR Report Compilation we planned and performed the work to provide limited assurance as to whether the BAE Systems' description of the Group compilation of the CR Report as outlined on the contents page in the section 'Report process' is not materially misstated. This provides less assurance and is substantially less in scope than reasonable assurance.

For the Woolf implementation, we planned and performed the work to obtain reasonable – not absolute – assurance as to whether the statement on the implementation of the Woolf Committee recommendations on pages 13-15 is a fair description of the progress made and actions taken to implement those recommendations.

What we did: key assurance procedures

Considering the risk of material error, we planned and performed the work to obtain all the information and explanations considered necessary to provide sufficient evidence to support our assurance conclusion. The key procedures we carried out were:

In relation to CR Report compilation:

- Interviewing managers at BAE Systems' head office responsible for CR management and reporting systems
- Gaining an understanding of BAE Systems' own process to collect information from issue owners (including subsidiary entities) and the process for collation and validation by the Group CR team

- Analysing and reviewing on a sample basis the key structures, systems, processes, procedures and controls relating to the Group level collation, validation and reporting processes of the CR report
- Reviewing the CR report against the findings of our work whilst assessing that the CR Report has been compiled as described on the contents page in the section 'Report process'; and
- The scope of our work did not include detailed testing of CR performance data or the operating effectiveness of processes and internal controls.

In relation to the implementation of the Woolf Committee recommendations:

- Interviewing programme management team to understand the processes and activities in place to control the Woolf programme
- Interviewing working group chairmen of the six key working groups, and a limited sample of working group team members, to understand the planned approach and actions taken to date to respond to the recommendations
- Interviewing a sample of senior executives, including the Steering Committee chairman and Project Management chairman to understand the commitment, drive and actions taken to date to address the recommendations
- Interviewing the chairman of the Project Management process to understand the approach to performing independent reviews of the project at key stages
- Observing a briefing given to the Ethical Points of Contact responsible for rolling out the Global Code of Conduct
- Interviewing a limited sample of members of the Company's legal department and legal advisers to understand the actions taken in relation to Business Development Adviser agreements
- Reviewing underlying documents to corroborate interview outcomes and inform our assessment of the statement on the implementation of the Woolf report recommendations; and
- The scope of our work did not include the provision of assurance over whether BAE System's programme of work is adequately designed to, or will, meet the requirements of the Woolf Report.

What we found: our assurance opinion

Limited assurance conclusion:

- Based on the assurance work performed nothing has come to our attention to suggest that the description on the contents page in the section 'Report Process' for compiling the Group CR Report is materially misstated.

Reasonable assurance opinion:

- BAE Systems' statement on the implementation of the Woolf Committee recommendations on pages 13-15 of their CR Report 2008, limited to statements made in the grey boxes under the headings Global Code of Conduct, Ethics helpline, Clear policies, Business Development Advisers, Implementing the Woolf Committee recommendations, Looking forward and the Woolf Committee – key facts is, in our opinion, in all material respects fairly stated as at 3rd April 2009.

Responsibilities of Directors and independent assurance provider

BAE Systems' responsibilities:

- The Directors are responsible for the preparation of the CR Report and for the information and statements contained in connection with it. They are responsible for determining BAE Systems' objectives in respect of CR performance and for establishing and maintaining appropriate performance management and internal control systems from which the reported information is derived.

Deloitte's responsibilities:

- Our responsibility is to independently express conclusions on the reliability of management's assertions on the selected subject matters as defined within the scope of work above
- This report is made solely to BAE Systems plc in accordance with our letter of engagement for the purpose of the directors' governance and stewardship. Our work has been undertaken so that we might state to the Company those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than BAE Systems plc for our work, for this report, or for the conclusions we have formed
- Our multi-disciplinary team of CR and assurance specialists performed the engagement in accordance with Deloitte's independence policies, which cover all of the requirements of the International Federation of Accountants (IFAC) Code of Ethics and in some areas are more restrictive. We confirm to BAE Systems that we have maintained our independence and objectivity throughout the year, including the fact that there were no events or prohibited services provided which could impair that independence and objectivity in the provision of this engagement.

Deloitte LLP

London, United Kingdom
3rd April 2009

Performance Summary

We collect data on business conduct, safety, environment, diversity and inclusion to help us monitor performance and identify areas for improvement. The data is recorded by our businesses and collated centrally for review. Specific notes are recorded below.

	2005	2006	2007	2008	
Economic					
Revenue	£11,019m	£12,333m	£14,309m	£16,671m	
Operating profit	£761m	£1,054m	£1,177m	£1,718m	
Equity dividends paid in year	£315m	£346m	£396m	£478m	
Wages and salaries	£2,989m	£3,274m	£3,353m	£4,053m	
Pension costs	£233m	£253m	£240m	£223m	
Employee numbers	100,100	88,600	97,500	106,400	
Business Conduct					
Ethics enquiries from employees	367	410	327	507	
Health, Safety and Environment					
Energy use (Gwh) ¹⁴	1,767	1,742	1,706	1,655	
CO2 emissions relating to energy use (million tonnes)	0.58	0.57	0.55	0.66	
Volatile organic compound emissions (tonnes) ¹⁴	610	742	642	519	
Major injuries recorded (per 100,000 employees)	55	47	48	68	
Days recorded lost to work-related injuries ¹⁵	8,774	10,204	10,084 ¹⁶	9,336	
Total recorded injuries to all employees	6,009	4,788	4,454	4,089	
Diversity and Inclusion¹⁷					
Gender diversity:	Male employees	81%	80%	79%	80%
	Female employees	19%	20%	21%	20%
Ethnic diversity ¹⁸ :	White	88%	87%	82%	85%
	Non-white	12%	13%	18%	15%
Age diversity:	Under 25	7%	7%	8%	10%
	26 to 35	18%	18%	17%	17%
	36 to 49	44%	42%	39%	38%
	50 to 59	25%	26%	27%	27%
	60+	6%	7%	9%	8%

14 Our environmental data reflects the emphasis on the minimisation of the use of resources within the Company's businesses. This reduction has been achieved even with an increase in throughput at a number of our sites.

15 The gap between Company performance and the external benchmark of 2,000 days lost per 100,000 employees was reduced by just over 9% during 2008.

16 We previously stated the 2007 figure as 8,734. This has been revised following a thorough review of baseline information.

17 The focus of our diversity agenda is creating an inclusive environment where our employees, regardless of gender, ethnicity or age, can realise their full potential.

18 Ethnic diversity figures are based on South Africa, UK and US data only.

This report has been printed by a company certified to ISO14001:2004.

The paper has been independently certified according to the rules of the Forest Stewardship Council (FSC). The cover contains 50% post consumer waste, 30% mill broke (mill recycled paper) and 20% virgin fibre. The text pages contain 50% recycled fibre and 50% virgin fibre. The pulp is bleached using an Elemental Chlorine Free (ECF) process.

This report is recyclable.

