Accounting principles and methods applied in preparation of the consolidated financial statements

General information

The consolidated financial statements of Henkel AG & Co. KGaA as of December 31, 2012 have been prepared in accordance with International Financial Reporting Standards (IFRS) and the relevant interpretations of the International Financial Reporting Interpretations Committee (IFRIC), as adopted per Regulation no. 1606/2002 of the European Parliament and the Council on the application of international accounting standards in the European Union, and in compliance with Section 315a of the German Commercial Code [HGB].

The individual financial statements of the companies included in the consolidation are drawn up on the same accounting date, December 31, 2012, as that of Henkel AG & Co. KGaA.

Members of the KPMG organization or other independent firms of auditors instructed accordingly have audited the financial statements of the material companies included in the consolidation. The Management Board of Henkel Management AG – which is the Personally Liable Partner of Henkel AG & Co. KGaA – compiled the financial statements on January 28, 2013 and approved them for forwarding to the Supervisory Board and for publication.

The consolidated financial statements are based on the principle of historical cost with the exception that certain financial instruments are accounted for at their fair values and pension obligations are measured using the projected unit credit method. The functional currency of Henkel AG & Co. KGaA and the reporting currency of the Group is the euro. Unless otherwise indicated, all amounts are shown in million euros. In order to improve the clarity and informative value of the consolidated financial statements, certain items are combined in the consolidated statement of financial position, the consolidated statement of income and the consolidated statement of comprehensive income, and then shown separately in the notes.

Scope of consolidation

In addition to Henkel AG & Co. KGaA as the ultimate parent company, the consolidated financial statements at December 31, 2012 include eight German and 169 non-German companies in which Henkel AG & Co. KGaA has a dominating influence over financial and operating policy, based on the concept of control. This is generally the case where Henkel AG & Co. KGaA holds, directly or indirectly, a majority of the voting rights. Companies in which not more than half of the voting rights are held are fully consolidated if Henkel AG & Co. KGaA, on the basis of contractual agreements or rights held, has the power, directly or indirectly, to appoint executive and managerial bodies and thereby to govern their financial and operating policies.

The following table shows the changes in the scope of consolidation compared to December 31, 2011:

Scope of consolidation

At January 1, 2012	**178**
Additions	9
Mergers	– 4
Disposals	– 5
At December 31, 2012	**178**

The changes in the scope of consolidation have not had any material effect on the main items of the consolidated financial statements.

Subsidiaries which are of secondary importance to the Group and to the presentation of a true and fair view of our net assets, financial position and results of operations due to their inactivity or low level of activity are generally not included in the consolidated financial statements. The total assets of these companies represent less than 1 percent of the Group's total assets; their total sales and income net of taxes are also less than 1 percent of the Group totals.

Acquisitions and divestments

The acquisitions and divestments made in fiscal 2012 had no material effect on the business and organizational structure of Henkel, nor on our net assets, financial position or results of operations.

Acquisitions

Effective January 2, 2012, we acquired control of the distribution company Bella Vista A/S, Silkeborg, Denmark. Our share of voting rights in the company is 100 percent. The purchase price paid was 5 million euros. This resulted in the recognition of goodwill amounting to 5 million euros.

In the first quarter, we spent 7 million euros acquiring the outstanding non-controlling interests in Chemofast Anchoring GmbH, Willich, Germany, increasing our shareholding as of March 1, 2012 from 73 percent to 95 percent. The difference between the previously held share of net assets and the purchase price has been recognized in retained earnings.

Effective August 1, 2012, we acquired the portfolio of high-performance pressure sensitive adhesives from Cytec Industries Inc., USA. The purchase price paid was 88 million euros, resulting in the recognition of goodwill of 51 million euros. It is assumed that the capitalized goodwill is completely tax-deductible. Incidental acquisition costs of 2 million euros were recognized in operating profit. Customer relationships were capitalized in the amount of 15 million euros. The fair value applied to the acquired trade accounts receivable is 9 million euros. If the high-performance pressure sensitive adhesives business we acquired had been included in the consolidated financial statements as of January 1, 2012, sales would have been 42 million euros higher and operating profit (EBIT) would have been 2 million euros higher.

In the second half of the year, we acquired the laundry cleaning business of Colgate-Palmolive in the Dominican Republic, paying a purchase price of 20 million euros. We have included the business in the consolidated financial statements since September 1, 2012. Trademarks with a fair value of 16 million euros were recognized, resulting in the recognition of goodwill amounting to 4 million euros.

In 2012, we spent 3 million euros on the acquisition of outstanding non-controlling interests in Rilken Cosmetics Industry S.A., Athens, Greece. Effective December 31, 2012, we increased our shareholding from 78 percent to 100 percent. The difference between the previously held share of net assets and the purchase price has been recognized in retained earnings.

The goodwill recognized in the year under review essentially represents the market position and profitability of the acquired businesses, together with expected synergies.

The purchase price allocation for all acquisitions was completed on December 31, 2012. The following table shows the acquisitions of subsidiaries in fiscal 2012. The acquisitions indicated, taken both individually and in sum, have not exerted any material effect on the net assets, financial position or results of operations of the Group.

Acquisitions 2012

January 1 to December 31 in million euros	Carrying amount	Adjustments	Fair value
Assets	**24**	**32**	**56**
Non-current assets	4	32	36
Current assets	20	–	20
Cash and cash equivalents	–	–	–
Liabilities	**3**	**–**	**3**
Non-current liabilities and provisions	–	–	–
Current liabilities and provisions	3	–	3
Net assets	**21**	**32**	**53**

Goodwill 2012

in million euros	Fair value
Purchase price	113
Fair value of non-controlling interests	–
Less net assets	53
Goodwill	**60**

Divestments

We realized 3 million euros in the third quarter from the sale of non-core activities attributable to the Adhesive Technologies business sector. The gain from the sale was 2 million euros.

The proceeds from the divestments indicated were received in cash. The gains were recognized under other operating income.

Consolidation methods

The financial statements of Henkel AG & Co. KGaA and of the subsidiaries included in the consolidated financial statements were prepared on the basis of uniformly valid principles of recognition and measurement, applying the standardized year-end date adopted by the Group. Such entities are included in the consolidated financial statements as of the date on which the Group acquired control.

All receivables and liabilities, sales, income and expenses, as well as intra-group profits on transfers of non-current assets or inventories, are eliminated on consolidation.

The purchase method is used for capital consolidation. With business combinations, therefore, all hidden reserves and hidden charges in the entity acquired are revalued at the time of acquisition, and fully reflected at fair value, and all identifiable intangible assets are separately disclosed if they are clearly separable or if their recognition arises from a contractual or other legal right. Any difference arising between the cost of acquisition and the (share of) net assets after purchase price allocation is recognized as goodwill. The goodwill of subsidiaries is measured in the functional currency of the subsidiary. Entities acquired are included in the consolidation for the first time as subsidiaries by offsetting the carrying amount of the respective parent company’s investment in them against their assets and liabilities. Contingent consideration is recognized at fair value as of the date of first-time consolidation. Subsequent changes in value do not result in an adjustment to the valuation at the time of acquisition. (Incidental) costs related to the acquisition of subsidiaries are not included in the purchase price. Instead, they are recognized in other operating charges in the period in which they occur. In the recognition of acquisitions of less than 100 percent, non-controlling interests are measured at the fair value of the share of net assets that they represent. We do not apply the option of measuring non-controlling interests at their fair value (full goodwill method).

In subsequent years, the carrying amount of the Henkel AG & Co. KGaA investment is eliminated against the current (share of) equity of the subsidiary entities concerned.

Changes in the shareholdings of subsidiary companies, as a result of which the participating interests of the Group decrease or increase without loss of control, are recognized within equity as changes in ownership without loss of control.

As soon as the control of a subsidiary is relinquished, all the assets and liabilities and the non-controlling interests, and also the accumulated currency translation gains or losses, are derecognized. In the event that Henkel continues to own non-controlling interests in the non-consolidated entity, these are measured at fair value. The result of deconsolidation is recognized under other operating income or charges.

Companies recognized at equity

Associated companies and joint ventures are recognized at equity.

An associated company is a company over which the Group can exercise material influence on the financial and operating policies without controlling it. Material influence is generally assumed when the Group holds 20 percent or more of the voting rights. Where a Group company conducts transactions with an associated company or a joint venture, the resulting gains or losses are eliminated in accordance with the share of the Group in that company.

Currency translation

The annual financial statements of the consolidated companies, including the hidden reserves and hidden charges of Group companies recognized under the purchase method, and also goodwill arising on consolidation, are translated into euros using the functional currency method outlined in International Accounting Standard (IAS) 21 "The Effects of Changes in Foreign Exchange Rates." The functional currency is the currency in which the foreign company predominantly generates funds and makes payments. As the functional currency for all the companies included in the consolidation is generally the local currency of the company concerned, assets and liabilities are translated at closing rates, while income and expenses are translated at the average rates for the year, based on an approximation of the actual rates at the date of the transaction. Equity items are recognized at historic exchange rates. The differences arising from using average rather than closing rates are taken to equity and shown as other components of equity or non-controlling interests, and remain neutral in respect of net income until the shares are divested.

In the subsidiaries' annual financial statements, transactions in foreign currencies are converted at the rates prevailing at the time of the transaction. Financial assets and liabilities in foreign currencies are measured at closing rates and recognized in profit or loss. For the main currencies in the Group, the following exchange rates have been used based on 1 euro:

Currencies

		Average exchange rate		Exchange rate on December 31	
	ISO code	2011	2012	2011	2012
Chinese yuan	CNY	8.99	**8.10**	8.16	**8.22**
Mexican peso	MXN	17.31	**16.90**	18.05	**17.19**
Russian ruble	RUB	40.91	**39.93**	41.77	**40.33**
Turkish lira	TRY	2.34	**2.31**	2.44	**2.36**
US dollar	USD	1.39	**1.28**	1.29	**1.32**

Recognition and measurement methods

Summary of selected measurement methods

Items in the consolidated statement of financial position	Measurement method
Assets	
Goodwill	Lower of carrying amount and recoverable amount (“impairment only” method)
Other intangible assets	
with indefinite useful lives	Lower of carrying amount and recoverable amount (“impairment only” method)
with definite useful lives	(Amortized) cost less any impairment losses
Property, plant and equipment	(Depreciated) cost less any impairment losses
Financial assets (categories per IAS 39)	
“Loans and receivables”	(Amortized) cost using the effective interest method
“Available for sale”	Fair value with gains or losses recognized directly in equity [1]
“Held for trading”	Fair value through profit or loss
“Fair value option”	Fair value through profit or loss
Other assets	(Amortized) cost
Inventories	Lower of cost and net realizable value
Assets held for sale	Lower of cost and fair value less costs to sell

[1] Apart from permanent impairment losses and effects arising from measurement in a foreign currency.

Liabilities	
Provisions for pensions and similar obligations	Present value of future obligations (projected unit credit method)
Other provisions	Settlement amount
Financial liabilities (categories per IAS 39)	
“Measured at amortized cost”	(Amortized) cost using the effective interest method
“Held for trading”	Fair value through profit or loss
Other liabilities	Settlement amount

The methods of recognition and measurement, which are basically unchanged from the previous year, are described in detail in the notes relating to the individual items of the statement of financial position on these pages. Also provided as part of the report on our financial instruments (Note 21 on pages 138 to 148) are the disclosures relevant to IFRS 7 showing the breakdown of our financial instruments by category, our methods for fair value measurement, and the derivative financial instruments that we use.

Changes in the methods of recognition and measurement arising from revised and new standards are applied retrospectively, provided that there are no alternative regulations that supersede the standard concerned. The consolidated statement of income from the previous year and the opening balance of the consolidated statement of financial position for this comparative period are adjusted as if the new methods of recognition and measurement had always been applied.

Accounting estimates, assumptions and discretionary judgments

Preparation of the consolidated financial statements is based on a number of accounting estimates and assumptions. These have an impact on the reported amounts of assets, liabilities and contingent liabilities at the reporting date and the disclosure of income and expenses for the reporting period. The actual amounts may differ from these estimates.

The accounting estimates and their underlying assumptions are based on past experience and are continually reviewed. Changes in accounting estimates are recognized in the period in which the change takes place where such change exclusively affects that period. A change is recognized in the period in which it occurs and in later periods where such change affects both the reporting period and subsequent periods. The judgments of the Management Board regarding the application of those IFRSs which have a significant impact on the consolidated financial statements are presented in the explanatory notes on taxes on income (Note 30 on pages 150 to 152), intangible assets (Note 1 on pages 120 to 123), pension obligations (Note 15 on pages 129 to 134), income tax provisions and other provisions (Note 16 on page 135), financial instruments (Note 21 on pages 138 to 148) and share-based payment plans (Note 33 on pages 153 to 154).

Essentially, discretionary judgments are made in respect of the following two areas:

- The US dollar liabilities of Henkel of America, Inc., Wilmington, USA, are set off against sureties of Henkel US LLC, Wilmington, USA, as the deposit and the loan are with the same lender and of the same maturity, there is a legal right to set off these sums, and the Group intends to settle net.
- The demarcation of the cash-generating units is also a discretionary judgment of the Group management and is explained under Note 1 on pages 120 to 123.

Application of IAS 8 “Accounting policies, changes in accounting estimates and errors”

In application of IAS 8 paragraph 41 et seq., the following information is reported:

On April 13, 2011, the European Commission imposed fines on a number of international laundry detergent manufacturers for reason of infringements that had occurred in various countries in Western Europe between 2002 and the beginning of 2005, which were discovered by Henkel in the course of internal compliance audits carried out in 2008. Henkel then immediately informed the relevant authorities and contributed materially to investigations into the matter. Due to our extensive cooperation with the EU Commission, Henkel was granted full immunity from fines.

On December 8, 2011, the French antitrust authorities imposed fines totaling around 360 million euros on several international detergent manufacturers on account of antitrust violations in France in the period from 1997 to 2004. Henkel received a fine of around 92 million euros. We have paid the amount and filed an action against the decision of the French antitrust authorities. In our opinion and in that of the attorneys from whom we are seeking advice, the French antitrust authorities’ decision is not legally correct. We cooperated extensively with the relevant authorities throughout the entire proceedings and, on the basis of our own internal investigations, supplied important information that assisted in establishing the key facts of the matter in France. In addition, we were the first company to disclose the European dimension of the case. In our understanding, the case in France is directly related to the antitrust violations concerning heavy-duty detergents in various Western European countries – including France – that led to sanctions being imposed by the European Commission on April 13, 2011 and in respect of which we were granted full exemption from sanctions. It would be contradictory if the French antitrust authorities were to impose separate sanctions on us in respect of these infringements.

In fiscal 2012, we reviewed the recognition made in the previous year. The review revealed that the recognition criteria of an asset were not present. We retain our legal position with no changes.

We have therefore subsequently restated the values from the previous year (2011) in the consolidated financial statement for 2012 and recognized the payment in other operating charges for 2011.

The restatement results in the effects shown in the following overview on items in the consolidated statement of financial position, the consolidated statement of income, the consolidated statement of comprehensive income and the consolidated statement of cash flows. We have also corrected the relevant details accordingly in the notes and the consolidated statement of changes in equity.

Application of IAS 8 “Accounting policies, changes in accounting estimates and errors”

in million euros	December 31, 2011 reported	Restatement	December 31, 2011 restated
Consolidated statement of financial position			
Other financial assets	748	– 92	656
Current assets	6,731	– 92	6,639
Total assets	18,579	– 92	18,487
Capital reserve	8,586	– 92	8,494
Equity attributable to shareholders of Henkel AG & Co. KGaA	8,641	– 92	8,549
Equity	8,762	– 92	8,670
Total equity and liabilities	18,579	– 92	18,487
Consolidated statement of income			
Other operating charges	– 92	– 92	– 184
Operating profit (EBIT)	1,857	– 92	1,765
Income before tax	1,702	– 92	1,610
Net income	1,283	– 92	1,191
– Attributable to shareholders of Henkel AG & Co. KGaA	1,253	– 92	1,161
One-time charges (additional voluntary information)	– 2	– 92	– 94
Consolidated statement of comprehensive income			
Total comprehensive income for the period	1,668	– 92	1,576
Total comprehensive income for the period, attributable to shareholders of Henkel AG & Co. KGaA	1,637	– 92	1,545
Earnings per share			
Earnings per ordinary share (basic)	2.88	– 0.21	2.67
Earnings per preferred share (basic)	2.90	– 0.21	2.69
Earnings per ordinary share (diluted)	2.87	– 0.21	2.66
Earnings per preferred share (diluted)	2.89	– 0.21	2.68
Consolidated statement of cash flows			
Operating profit (EBIT)	1,857	– 92	1,765
Change in other assets	– 71	+ 92	21

New international accounting regulations according to International Financial Reporting Standards (IFRS)

Accounting methods applied for the first time in the year under review

Accounting methods applied for the first time in the year under review

	Significance
IFRS 7 (Amendment) "Disclosure Requirements for Transfers of Financial Assets" – application as of July 1, 2011	irrelevant
IAS 12 (Amendment) "Recovery of Underlying Assets" – application as of January 1, 2012	irrelevant
IFRS 1 (Amendment) "Severe Hyperinflation and Removal of Fixed Dates for First-time Adopters" – application as of July 1, 2011	irrelevant

- In October 2010 the International Accounting Standards Board (IASB) published amendments to IFRS 7 "Financial Instruments: Disclosures." The purpose of the extended disclosure requirements is to provide financial statement users with a better understanding of the relationship between the transferred financial assets and the corresponding liabilities. Particularly where financial assets are completely derecognized, the additional information now required should enable an assessment of the type and the risks of any continuing involvement.
- In December 2010, the IASB published amendments to IAS 12 "Income Taxes." The amendment concerns the treatment of temporary tax differences related to investment property. It clarifies that the valuation of deferred taxes must proceed based on the rebuttable assumption that the amount will be reversed through sale.

The first-time application of the amended standards had no material impact on the presentation of our financial statements.

Accounting regulations not applied in advance of their effective date

The following standards and amendments to existing standards of possible relevance to Henkel, which have been adopted into EU law (endorsement mechanism) but are not yet mandatory, have not been applied early:

Accounting regulations not applied in advance of their effective date

	Mandatory for fiscal years beginning on or after
IAS 32 (Amendment) "Offsetting Financial Assets and Liabilities"	January 1, 2014
IFRS 7 (Amendment) "Disclosures – Offsetting Financial Assets and Liabilities"	January 1, 2013
IAS 1 (Amendment) "Presentation of Items of Other Comprehensive Income"	July 1, 2012
IAS 19 revised "Employee Benefits"	January 1, 2013
IAS 28 (Amendment) "Investments in Associates and Joint Ventures"	January 1, 2014
IFRS 10 "Consolidated Financial Statements"	January 1, 2014
IFRS 11 "Joint Arrangements"	January 1, 2014
IFRS 12 "Disclosure of Interest in Other Entities"	January 1, 2014
IFRS 13 "Measurement of Fair Value"	January 1, 2013

- In December 2011, the IASB published amendments to IAS 32 "Financial Instruments: Presentation" and IFRS 7 "Financial Instruments: Disclosures." The amendment to IAS 32 explains and clarifies the criteria for offsetting financial assets and financial liabilities in the statement of financial position. Along with this clarification, the explanatory notes in IFRS 7 were also expanded. The amendment to IAS 32 is mandatory for financial years beginning on or after January 1, 2014. The amendment to IFRS 7 is mandatory for financial years beginning on or after January 1, 2013.
- In June 2012, the IASB published amendments to IAS 1 "Presentation of Financial Statements." In the future, items of other comprehensive income in the consolidated statement of comprehensive income which are later reclassified ("recycled") to the statement of income must be presented separately from items of other comprehensive income which will never be reclassified. The change is first applicable for financial years beginning on or after July 1, 2012.
- In June 2011, the IASB published amendments to IAS 19 "Employee Benefits" (IAS 19, revised 2011). Henkel expects that the following changes will affect the consolidated financial statements: IAS 19 (revised) replaces the expected income from plan assets and the interest expense on the pension obligation with a uniform net interest component.

In addition, IAS 19 (revised) provides for recognition in profit and loss of non-vested past-service costs as they occur. The disclosure and explanation requirements are also expanded. The announcement is applicable for financial years beginning on or after January 1, 2013. IAS 19 (revised) requires retrospective application and the presentation of the effects of the first-time application on the opening balance at January 1, 2012. Henkel expects no material effects from this for the items "Total comprehensive income for the period" and "Equity." The net interest component for fiscal 2012 will increase as a result of IAS 19 (revised) by around 40 million euros. In fiscal 2013, the net interest component will approach the level of the adjusted 2012 fiscal year.

- In May 2011, the IASB published the new standards IFRS 10 "Consolidated Financial Statements," IFRS 11 "Joint Arrangements," and IFRS 12 "Disclosure of Interest in Other Entities" as well as amendments to IAS 28 "Investments in Associates." Under the new concept of IFRS 10, control exists when the potential parent company holds decision power over the potential subsidiary based on voting rights or other rights, it is exposed to positive and negative variability in returns from the subsidiary, and these returns may be affected by the decision power held by the parent. Under the new concept of IFRS 11, a distinction is made in a joint arrangement as to whether it is a joint operation or a joint venture. In a joint operation, the individual rights and obligations are accounted for proportionately in the consolidated financial statements. In contrast, joint ventures are represented in the consolidated financial statements using the equity method. As part of the adoption of IFRS 11, adjustments were also made to IAS 28. The new IFRS 12 expands the disclosure requirements for interests in other entities. The new standards and the amendments to standards must be applied beginning January 1, 2014.
- IFRS 13 "Fair Value Measurement," which was published in May 2011, provides for the uniform measurement of fair value in IFRS financial statements. Fair value is defined as exit price, meaning the price that would be realized in the sale of an asset or the price that would have to be paid to transfer an obligation. IFRS 13 is mandatory for financial years beginning on or after January 1, 2013.

These new standards and amendments to existing standards will be applied by Henkel from fiscal year 2013 or later. Unless otherwise indicated, we expect the future application of the aforementioned regulations not to have a significant impact on the presentation of the financial statements.

Accounting regulations not yet adopted into EU law

In fiscal 2012, the IASB issued the following standards and amendments to existing standards of relevance to Henkel, which still have to be adopted into EU law ("endorsement mechanism") before they become applicable:

Accounting regulations not yet adopted into EU law

	Mandatory for fiscal years beginning on or after
General standard "Improvements to IFRS 2009–2011"	January 1, 2013
IFRS 1 (Amendment) "Government Loans"	January 1, 2013
IFRS 9 "Financial Instruments"	January 1, 2015
IFRS 7 (Amendment) and IFRS 9 (Amendment) "Mandatory Effective Date and Transition Disclosure"	January 1, 2015
IFRS 10 (Amendment), IFRS 11 (Amendment) and IFRS 12 (Amendment) "Transition Guidance"	January 1, 2014
IFRS 10 (Amendment), IFRS 12 (Amendment) and IAS 27 (Amendment) "Investment Companies"	January 1, 2014

These standards and amendments to existing standards will be applied by Henkel starting in 2013 or later.