

Corporate governance

Compliance

Corporate governance has been and remains the responsibility of the whole Board. This statement describes how the Company applies the principles and complies with the provisions of the Combined Code on Corporate Governance published in June 2006, which applied to the Company in respect of the financial year ended 31st December 2008. The Board considers that, subject to the explanation of the ratio of executive and non-executive directors below, the Company met the requirements of the Combined Code throughout the year ended 31st December 2008. The Board assesses on an on-going basis its practices to ensure continued compliance with the Combined Code and has allocated responsibility for compliance to appropriate directors or officers. Contact has been made with major shareholders to allow discussion of the Company's governance policy and strategy with the Chairman and the Senior Independent Director.

Board composition and procedures

During the year the Board comprised the non-executive Chairman, three independent non-executive directors, including a Senior Independent Director, and five executive directors, details of whom are set out on pages 28 to 30. During the year the positions of Chairman, Chief Executive and Senior Independent Director were held by separate individuals. There is a clear written division of responsibility between the Chairman and the Chief Executive. The ratio of executive to non-executive directors is currently considered to be the best structure for the Company. The Board is responsible for the Group's business operations and five executive directors are present on the Board in order to provide first-hand information and contributions to the running of the business. The executive directors control the Group's devolved management structure which requires local management initiative across the Group's global spread of operating companies, its broad product range and wide customer base. Board membership of the executives is key to the overall management of the Group which employs a relatively flat management structure. This also provides the non-executive directors with regular direct access to the full executive management team. The Company views this to be a very appropriate and successful mix; appointing additional non-executive directors would make the Board more cumbersome and would not add to the quality of the Board's performance. The divisional structure will be retained with additional senior managers appointed as regional general managers to provide support in each of the divisions.

The Board applies an appropriate policy in the recruitment of independent non-executive directors to meet the particular requirements of the Board. Each of the non-executive directors has a letter of appointment which meets the requirements of the Combined Code. The non-executive directors have all had senior executive experience and offer independent judgement on Board matters. The non-executive directors of the Company, including the Chairman, do not participate in any bonus, share option or share ownership schemes and their appointments are non-pensionable.

The Board normally meets six times per year to consider strategic developments and to review trading results and operational and business issues. All directors attended all meetings either in person or by telephone in 2008. In particular the Board deals with those matters reserved to it for decision, details of which are posted on the Group web site: www.SpiraxSarcoEngineering.com and are as follows:

(i) Management

- Approval of Group strategy and annual plans.
- Commitments relating to the acquisition or disposal of any company or business by the Group.
- Material or unusual contracts.
- Capital expenditure items in excess of £500,000 or such other limit agreed by the Board. Items over £250,000 but less than £500,000 are reported to the Board.

(ii) Board membership and board committees

- The formal appointment and dismissal of directors.
- Terms of reference and membership of Board Committees.

(iii) Corporate governance/accounting

- Approval of actions requiring the production of public documents including circulars to shareholders, related documents and press releases.
- Approval of accounting policies or practices, including the Treasury policy.
- Individual borrowings, financial instruments, guarantees or provision of equity capital, beyond the authority of the Finance Committee.
- Approval of the content of the Annual Report and Accounts, the Half Year Report and Interim Management Statements.
- Appointment and dismissal of the Company Secretary.
- Through the Audit Committee, remuneration of auditors and recommendation for appointment and removal of auditors.
- Dividend policy, interim dividends and proposed final dividends.
- Any matter to be dealt with at an annual general meeting or extraordinary general meeting.

(iv) Other

- Significant alterations to existing Group Risk Management policies relating to insurance, environmental and health and safety matters.
- Changes in principal professional advisers.
- Major changes to pension and employee share schemes operated in the Group.
- Prosecution, defence or settlement of any material litigation.

All directors receive detailed Board papers and reports one week prior to each Board meeting. There is provision for the non-executive directors to meet together both with and without the Chairman.

Utilising a format created with the advice of Towers Perrin, the Board again carried out a rigorous evaluation of Board performance in accordance with the Combined Code requirements which confirmed the effective operation of the Board and reflected the importance of strategic matters. The evaluation process comprises a review conducted by the Company Secretary and reported to the Chairman of all directors' views on the operation of the Board and the performance of the Chairman, the Chairman's and Chief Executive's review of the Board performance of each director, the Chairman's review of the non-executive directors and the review by Committee members and attendees of the operations of the Audit, Nomination and Remuneration Committees and the performance of the Chairman of each of those Committees. The evaluation confirmed a continued high rating for the Board's operations and encompassed Board constitution, Board meetings, Board functionality, communication and knowledge management, Company secretariat performance, assessment of the Chairman's performance and the effectiveness of the Board's Committees.

There are procedures for individual Board members to receive induction and training as appropriate and provision to solicit independent professional advice at the Company's expense where specific expertise is required in the course of exercising their duties. All directors have access to the Company Secretary, who is responsible for ensuring compliance with applicable legislative and regulatory requirements.

The Company provides directors' and officers' insurance for Board members and the directors of Group companies.

All directors are subject to re-appointment by shareholders at the first opportunity after their appointment and thereafter at intervals of no more than three years.

Conflicts

The Company amended its articles of association in May 2008 to deal with, amongst other things, the provisions on conflicts of interest in the Companies Act 2006 which came into force in October 2008. Following this, the Company has put in place procedures for the disclosure and review of any conflicts, or potential conflicts, of interest which the directors may have and for the authorisation, where considered appropriate, of such conflict matters by the Board. In deciding whether to authorise a conflict or potential conflict the directors must have regard to their general duties under the Companies Act 2006. The authorisation of any conflict matter, and the terms of authorisation, may be reviewed at any time and will be reviewed formally by the Board on an annual basis.

Senior independent director

During the year Mr. W. H. Whiteley was the Senior Independent Director.

Committees

The Board delegates specific responsibility to Board Committees, notably the Audit, Nomination and Remuneration Committees, in line with best practice. The terms of reference for these Committees are posted on the Group web site: www.SpiraxSarcoEngineering.com. In the period from the beginning of the year until 31st March 2008 the Finance Committee comprised Messrs. M. Townsend (Chairman), M. J. D. Steel and D. J. Meredith. With effect from 1st April 2008 the Finance Committee comprised Messrs. M. Townsend (Chairman), M. E. Vernon and D. J. Meredith. The Risk Management Committee is composed of the executive directors and the Company Secretary.

(i) Audit committee

The Audit Committee comprised Messrs. W. H. Whiteley (Chairman), G. Bullock and E. Lindh. All members are independent in accordance with the independence criteria set out in the Combined Code. There were four meetings of the Audit Committee during the year and all members attended all meetings, with the exception of Mr. G. Bullock who was unavailable for one meeting.

A summary of the Audit Committee's duties and responsibilities is set out on page 36.

(ii) Nomination committee

In the period from the beginning of the year until 31st March 2008 the Nomination Committee comprised Messrs. M. Townsend (Chairman), G. Bullock, E. Lindh, M. J. D. Steel and W. H. Whiteley. With effect from 1st April 2008 the Nomination Committee comprised Messrs. M. Townsend (Chairman), G. Bullock, E. Lindh, M. E. Vernon and W. H. Whiteley. There were two meetings of the Nomination Committee and all members attended both meetings.

The Nomination Committee proposes to the Board new appointments for both executive and non-executive directors and determines on an individual basis the most appropriate method of identifying suitable applicants. The Nomination Committee arranges for the executive directors' views to be assessed before an appointment decision is made. The Nomination Committee fully followed this process in the appointment of Dr. K. Rajagopal as non-executive director and Mr. M. E. Gibbin as an executive director.

(iii) Remuneration committee

The Remuneration Committee comprised Messrs. W. H. Whiteley (Chairman), G. Bullock and E. Lindh. All members are independent in accordance with the independence criteria set out in the Combined Code. There were four meetings of the Remuneration Committee and all members attended all meetings, with the exception of Mr. G. Bullock who was unavailable for one meeting.

The Directors' Remuneration Report presented by the Board of Directors is set out on pages 42 to 49.

The Company Secretary acts as Secretary to the Audit, Nomination and Remuneration Committees.

Shareholder relations

The Group conducts regular dialogue with institutional shareholders and provides such information as is permitted within the guidelines of the Listing Rules. In particular major shareholders have been approached with a view to discussing the Company's governance and strategy with the Chairman and Mr. W. H. Whiteley, the Senior Independent Director. As required by major shareholders, the Senior Independent Director is available to listen to their views on any areas of concern they may have. There were no requests received from shareholders for meetings with the Chairman or the non-executive directors during 2008. Reports are made to the Board of all meetings with major shareholders and analysts including, in particular, briefings after half year and final results.

The preliminary results announcement may be accessed by investors on the Group web site: www.SpiraxSarcoEngineering.com. The Annual Report and Accounts is also posted on the web site: www.SpiraxSarcoEngineering.com.

All shareholders are invited to participate in the annual general meeting, where the chairmen of the Audit, Nomination and Remuneration Committees will be available to answer questions. The results of proxy votes are declared at annual general meetings after each resolution has been dealt with on a show of hands. Details of the proxy votes received will be published on the Group web site: www.SpiraxSarcoEngineering.com, following the annual general meeting.

Internal controls

The Board has overall responsibility for the system of internal controls and for reviewing its effectiveness, whilst the role of management is to implement Board policies on risk and control. There is an ongoing process for identifying and managing risks faced by the Group which has been in place for the year under review and up to the date of approval of the Annual Report and Accounts. The reviews cover all material controls, including financial, operational and compliance controls and risk management systems. The system of internal controls is designed to manage rather than eliminate the risk of failure to achieve the business objectives.

The Board believes from its reviews that the system of internal controls is embedded in the business and regular review allows for assessment of new and changing risks in the Group's business.

In pursuing these objectives, internal controls can provide only reasonable and not absolute assurance against material misstatement or loss.

Corporate governance continued

As required by the UK Listing Authority, the Company has complied throughout the year and up to the date of this report with the Combined Code provisions on internal controls having established the procedures necessary to implement the guidance issued by the Turnbull Committee and by reporting in accordance with that guidance.

(i) Risk management

The Group has operated procedures for considering risks in the normal operations of the Group and with regard to significant transactions. Strategic and annual planning also encompass consideration of business risks. The Risk Management Committee specifically reviews any risks facing the business which could give rise to a significant loss.

The Risk Management Committee carried out a review with external consultants, Marsh Ltd, of the risk register and risk management process in the context of the current business structure and operations with the aim of validating the risk register and the general risk management process and identifying any additional new risks which could involve a significant risk to the Group's business. This exercise was completed early in 2008 and consisted of a review of the risk magnitude and risk likelihood. Significant potential new risks were assessed and countermeasures established. The Board, on Marsh Ltd's advice, is satisfied that the system of management for significant risks is appropriate for the Group and is properly executed.

As part of the risk management process, Group companies are required to report on a six monthly basis their position with regard to implementing identified countermeasures to address the Group's significant business risks. The six monthly returns are assessed by the Risk Management Committee and the results of that assessment are reported by the Company Secretary to the Audit Committee. The Risk Management Committee carries out an annual review of the business risks. The Audit Committee monitors the system of reporting and its effectiveness as a whole and reports to the Board with its review of the assessments made by the Risk Management Committee and any recommendations for improvements to the process.

In the UK the operation of the Incident Management Team, which deals with the situation immediately after any major incident, was reviewed and the Team strengthened. The manufacturing operation in France has completed a business continuity planning exercise and business continuity planning exercises are also being undertaken by a number of Group companies, notably Spirax Sarco Inc. and Spirax-Sarco Srl in Italy.

(ii) Financial

The Finance Committee of the Board considers financing and investment decisions concerning the Group, including the giving of guarantees and indemnities, and monitors policy and control mechanisms for managing treasury risk within the limits laid down by the Board.

Financial reporting systems include comprehensive annual plans approved by the Board and monthly reporting of actual results with appropriate comparisons against plan and previous year's results. Forecast operating results for the year are regularly updated. Capital investment is subject to approval under a clear policy. This includes annual plans, appropriate authorisation, detailed investment appraisal and post-investment review and due diligence requirements where businesses are being acquired.

(iii) Operational

All Group companies are required to complete self-certification questionnaires regarding compliance with the policies, procedures and minimum requirements for an effective system of internal controls. Self-certification is given by both the general manager and the finance manager of the operation.

(iv) Audit committee

The Audit Committee considers the appropriateness and effectiveness of the Group's internal controls, policies and procedures and the outcome of the external audit for the year. The Committee also reviewed the outcome of internal audit reports and risk management returns during the year. Its meetings are normally attended by the Finance Director, the external auditors and, at the invitation of the Committee, the Chairman. There is provision for the Committee to confer with the auditors without the attendance of executive directors. The Audit Committee reviews the independence of the external auditors on an annual basis.

The Committee considers in detail reports prepared by the auditors in relation to the half year and final accounts and accounting practices and developments. It also considers reports and explanations provided by the Finance Director.

The Board has approved terms of reference for the Audit Committee meeting the requirements of the Combined Code. The Audit Committee's responsibilities include:

- monitoring the integrity of the accounts and in particular reviewing the Group's internal controls, risk management framework and internal audit reports;
- reviewing the scope and results of the auditors' work, their independence and objectivity and audit fee;
- recommending the appointment, re-appointment or removal of external auditors; and
- reviewing the accounting policies and practices of the Company and at the end of the annual audit cycle, assessing the effectiveness of the audit process.

The Audit Committee reviewed and noted compliance with the good practice list of matters established by the Audit Committee Institute in all material matters.

(v) Non-audit services

A policy on non-audit services provided by the auditors in line with professional practice has been established and approved by the Audit Committee. The external auditors have undertaken non-audit work (in regard to taxation and acquisition due diligence) and the fees paid by the Company for it are set out in Note 6 on page 61. The scope and extent of non-audit work undertaken by the Company's auditors is carefully controlled in line with the written terms provided by the Company to the auditors with the objective of avoiding impact on their independence and objectivity. In particular, the auditors are prohibited from providing services in relation to valuations, recruitment, dispute resolution and accounting services. The Audit Committee monitors the scope of the auditors' work, and specific approval from the Committee Chairman or the full Audit Committee is required for fees over established thresholds.

(vi) Whistle blowing

If any employee in the Group has reasonable grounds for believing that the Group Business Code or Management Code is being breached by any person or group of people and does not feel able to voice the matter with his or her manager, he or she is able to contact the Company Secretary in Cheltenham with full details. The Company Secretary will ensure that (a) the circumstances are properly investigated and (b) the employment of the person contacting the Company Secretary will be protected appropriately.

Internal audit

Following a review in 2006, the Board established an enhanced internal audit function which allows each of the Group companies to be audited at least every four years. All businesses acquired by the Group are subject to internal audit within one year from the date of acquisition. Internal audit resource is supplemented by experienced qualified accounting staff from principal Group companies and a professional auditing firm, BDO Stoy Hayward LLP. Reports are made to the Audit Committee and the Board as a whole. The implementation of the internal audit function has been successfully achieved and no significant matters were raised in the reports made in the 16 subsidiaries audited during the year.

Going concern

The Group's business activities, together with the main trends and factors likely to affect its future development, performance and position, and the financial position of the Group, its cash flows, liquidity position and borrowing facilities, are set out in the Business Review on pages 10 to 27. In addition Note 33 on pages 81 to 85 to the financial statements includes the Group's objectives, policies and processes for managing its capital, its financial risk management objectives, details of its financial instruments and hedging activities, and its exposures to credit risk and liquidity risk.

The Group has considerable financial resources together with contracts with a diverse range of customers and suppliers across different geographic areas and industries. No one customer accounts for more than 1% of Group turnover. As a consequence, the directors believe that the Group is well placed to manage its business risks successfully despite the current uncertain economic outlook.

After making enquiries and after conducting a formal review of the Group's financial resources at their October Board Meeting, the directors have a reasonable expectation that the Company and the Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

Directors' responsibilities

The Statement of Directors' Responsibilities is set out on page 50.