

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 2008 (the Combined Code), which applied to the Company in respect of the financial year ended 31st December 2009 and is publicly available at www.frc.org.uk. The Listing Rules of the Financial Services Authority require UK listed companies to report on the manner in which they apply the Combined Code. The Board considers that, subject to the ratio of executive and non-executive directors and the composition of the audit and remuneration committees from the beginning of the year until 9th February 2009 and from 1st July to 16th July (each of which is explained below), the Company met the requirements of the Combined Code throughout the year ended 31st December 2009. 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 three major shareholders availed themselves of the opportunity to meet the Chairman.

Disclosures required under DTR 7.2.6 can be found on page 34.

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 30 and 31. 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 regional general managers providing 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 all have or have 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 met six times in the 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 2009, with the exception of Mr. C. G. Watson who was unavailable for two meetings. In particular the Board deals with those matters reserved to it for decision, details of which are posted on the Group website: www.SpiraxSarcoEngineering.com and are as follows:

(i) Accounts and audit

- Approval of preliminary and annual reports and accounts, half-yearly reports and interim management statements.
- Accounting policies and practices and any changes thereto; the use of any off-balance sheet structures.
- Acceptance of any proposed audit qualification of the accounts.
- Approval of Audit Committee's recommendations for appointment or removal of external auditors.

(ii) Strategic and policy considerations

- Review and approve the Group's overall corporate strategy and annual business plan.
- Changes related to the Company's status as a listed company or major structural changes to the Group.
- Agreement of codes of ethics and business practice, in light of the directors' duty to promote the success of the Company for the benefit of the members as a whole, and in doing so having regard (amongst others) to:
 - the likely consequences of any decision in the long term,
 - the interests of the Company's employees,
 - the need to foster the Company's business relationships with suppliers, customers and others,
 - the impact of the Company's operations on the community and the environment,
 - the desirability of the Company maintaining a reputation for high standards of business conduct, and
 - the need to act fairly as between members of the Company.
- Appointment of, or changes to, principal professional advisers.
- Environmental policy.
- Health and safety policy.
- Any matter which could reasonably be expected to have a material effect on the reputation or standing of the Group.

(iii) Risk management

- Reviewing the effectiveness of risk management and internal control on an ongoing basis, including receiving and reviewing regular reports on internal control.
- Carrying out an assessment (at least annually) of significant risks and effectiveness of risk management and internal control policies; and reporting to shareholders on such matters.
- Prosecution, defence or settlement of litigation, arbitration or other proceedings material to the Company/Group and, for this purpose, litigation, arbitration or other proceedings shall be deemed material if the proceedings are for an amount in excess of £5 million or if the penalty likely to be suffered may exceed £5 million.

(iv) Transactions

- Major investment and capital projects in excess of £1 million. Investments or projects in excess of £500,000 sanctioned by the Executive team will be reported to the Board.
- Acquisitions and disposals of subsidiaries.
- Acquisitions and disposals of other assets or liabilities above £1 million.
- Material contracts which are in the ordinary course of business with a value of above £1 million.
- Contracts not in the ordinary course of business.
- Contracts in which a director or other related party is interested.
- Any binding commitment to enter into a material strategic alliance, joint venture, partnership or profit sharing arrangement.
- Giving security over significant assets.

(v) Finance

- Approval of Treasury Policy or amendments thereto.
- Approval of any financing or currency arrangement above the limit of the Finance Committee.

Corporate governance continued

(vi) Regulatory requirements

- Ensuring compliance with the Listing, Prospectus, Disclosure and Transparency Rules.
- Approval of all circulars, prospectuses and equivalent documents (save that approval of routine documents may be delegated to a committee).
- Approval of announcements concerning matters decided by the Board.
- Delegation of authority to issue an urgent announcement without the need to call a Board meeting, in order to comply with the Company's regulatory obligation to announce inside information as soon as possible.
- Dividend policy, approval of the interim dividend and recommendation of the final dividend.
- Calling general meetings of shareholders.
- Setting of general Group policy on charitable and political donations.
- Issue of shares or other securities (other than on notice of exercise of employee share options) or repurchase of shares.
- Changes relating to the Company's share capital.

(vii) Directors and senior employees

- Approval of Nomination Committee's recommendations on:
 - Board appointments and removals;
 - Board succession;
 - appointment of Chairman and terms of engagement (other than remuneration) for Chairman;
 - terms of engagement (other than remuneration) of non-executive directors;
 - the re-appointment of any non-executive director at the end of the specified term of office;
 - the re-election by shareholders of any director; and
 - any matters concerning the continuation in office of any director at any time.
- Remuneration of non-executive directors.
- Terms of engagement (other than remuneration package) of executive directors.
- Appointment and removal of Company Secretary.
- Board policy on the duration of contracts with directors (both executive and non-executive).
- The procedures in place (or to be put in place) for the authorisation of directors' conflict matters falling within section 175 of the Companies Act 2006 and any changes to these procedures.
- The authorisation of any conflict matter arising for any director of the Company under section 175 of the Companies Act 2006 and the terms and conditions attaching to such authorisation.
- Terms of reference and membership of Board committees.
- Delegation of the Board's powers.
- Procedure for directors in the furtherance of their duties to take independent professional advice, at the Company's expense.
- Assessment of which non-executive directors are independent.
- Approval of training and development programmes for directors as relating to their duties as directors.
- Approval of performance evaluation programmes for Board, committees and individual directors.

(viii) Employment issues

- Major changes in the rules or funding of the pension schemes.
- Major changes in employee or directors' share schemes and major changes in the allocation of share options.

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 without any executive directors present (both with and without the Chairman).

All other matters not reserved to the Board for decision are delegated appropriately.

Utilising a format created with the advice of Towers Perrin (now Towers Watson), 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. Improvements are made to the Board's operation as a result of the evaluation.

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, together with senior officers.

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

From 1st October 2008, the directors became subject to a statutory duty under the Companies Act 2006 to avoid a situation where they have, or could have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the Company. Directors of public companies may authorise conflicts and potential conflicts where appropriate, if the articles of association contain a provision to this effect. 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. The Company has established formal procedures for the disclosure and review of any conflicts, or potential conflicts, of interest which the directors may have and for the authorisation 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. The Board believes that the procedures established to deal with conflicts of interest are operating effectively.

Senior independent director

Mr. G. Bullock succeeded Mr. W. H. Whiteley as the Senior Independent Director on 1st July 2009.

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 website: www.SpiraxSarcoEngineering.com. In the period from the beginning of the year until 30th June 2009 the Finance Committee comprised Mr. M. Townsend (Chairman), Mr. M. E. Vernon and Mr. D. J. Meredith. With effect from 1st July 2009 the Finance Committee comprised Mr. W. H. Whiteley (Chairman), Mr. M. E. Vernon and Mr. D. J. Meredith. The Risk Management Committee is composed of the five executive directors and the Company Secretary.

(i) Audit committee

From 1st January until 9th February 2009, the Audit Committee comprised Mr. W. H. Whiteley (Chairman) and Mr. G. Bullock; from 10th February until 30th June, the Committee comprised Mr. W. H. Whiteley (Chairman), Mr. G. Bullock and Dr. K. Rajagopal. From 1st July to 16th July, the Committee comprised Mr. G. Bullock and Dr. K. Rajagopal and from 17th July to 31st December 2009, the Committee comprised Mr. C. G. Watson (Chairman), Mr. G. Bullock and Dr. K. Rajagopal.

During the periods 1st January to 9th February and 1st July to 16th July 2009 the Company did not fully comply with provision C.3.1 of the Combined Code as the Audit Committee comprised two independent non-executive directors. There were three meetings of the Audit Committee during the year and all members attended all meetings, with the exception of Mr. C. G. Watson who was unavailable for one meeting. All members are independent in accordance with the independence criteria set out in the Combined Code.

A summary of the Audit Committee's duties and responsibilities is set out on page 38.

(ii) Nomination committee

From 1st January until 9th February 2009, the Nomination Committee comprised Mr. M. Townsend (Chairman), Mr. G. Bullock, Mr. M. E. Vernon and Mr. W. H. Whiteley; from 10th February until 30th June, the Committee comprised Mr. M. Townsend (Chairman), Mr. G. Bullock, Dr. K. Rajagopal, Mr. M. E. Vernon and Mr. W. H. Whiteley. From 1st July to 16th July, the Committee comprised Mr. W. H. Whiteley (Chairman), Mr. G. Bullock, Dr. K. Rajagopal and Mr. M. E. Vernon and from 17th July to 31st December 2009, the Committee comprised Mr. W. H. Whiteley (Chairman), Mr. G. Bullock, Dr. K. Rajagopal and Mr. C. G. Watson. There were three meetings of the Nomination Committee and all members attended all meetings, with the exception of Dr. K. Rajagopal who was unavailable for one meeting.

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 Mr. C. G. Watson as non-executive director.

(iii) Remuneration committee

From 1st January until 9th February 2009, the Remuneration Committee comprised Mr. W. H. Whiteley (Chairman) and Mr. G. Bullock; from 10th February until 30th June, the Committee comprised Mr. W. H. Whiteley (Chairman), Mr. G. Bullock and Dr. K. Rajagopal. From 1st July to 16th July, the Committee comprised Mr. G. Bullock (Chairman) and Dr. K. Rajagopal and from 17th July to 31st December 2009, the Committee comprised Mr. G. Bullock (Chairman), Dr. K. Rajagopal and Mr. C. G. Watson.

During the periods 1st January to 9th February and 1st July to 16th July 2009 the Company did not fully comply with provision B.2.1 of the Combined Code as the Remuneration Committee comprised two independent non-executive directors. There were two meetings of the Remuneration Committee and all members attended both meetings. All members are independent in accordance with the independence criteria set out in the Combined Code.

In determining the remuneration paid to directors, the Remuneration Committee was advised by Towers Perrin.

The Directors' Remuneration Report presented by the Board of Directors is set out on pages 39 to 45.

(iv) Risk management committee

In the period from the beginning of the year until 30th April 2009, the Risk Management Committee comprised Mr. M. E. Vernon, Mr. A. D. H. Black, Mr. N. H. Daws, Mr. D. J. Meredith, Mr. A. J. Scrivin and Mr. W. G. Stebbings. With effect from 1st May 2009, the Risk Management Committee comprised Mr. M. E. Vernon, Mr. N. H. Daws, Mr. M. E. Gibbin, Mr. D. J. Meredith, Mr. A. J. Scrivin and Mr. W. G. Stebbings.

There were three meetings of the Risk Management Committee and all members attended all meetings with the exception of Mr. M. E. Gibbin who was unavailable for one meeting. Prior to his appointment, Mr. M. E. Gibbin attended two meetings on the invitation of the Committee. In addition to reviewing the risk management returns provided by Group companies at 30th June 2009 and 31st December 2009 and reporting on the results of these returns to the Board, the Committee also conducted a review of the Group's risk registers to ensure the continuing applicability and relevance of the registers.

The terms of reference for each of the Audit, Nomination and Remuneration Committees can be viewed in the Corporate Governance section of the Group website: www.SpiraxSarcoEngineering.com.

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. G. Bullock, 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. Following his appointment as Chairman, Mr. W. H. Whiteley offered major shareholders the opportunity of a meeting and, as a result, meetings were held with three major shareholders. 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 website: www.SpiraxSarcoEngineering.com. The Annual Report and Accounts is also posted on the website: 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 website: 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, and assess the effectiveness of, all material controls, including financial, operational and compliance controls and risk management systems. This ensures that proper accounting records have been maintained, that financial information used within the business is reliable and that the consolidated accounts preparation and financial reporting process comply with all relevant regulatory reporting requirements. 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 annual 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.

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 (which is publicly available at www.frc.org.uk).

(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 material 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

Corporate governance continued

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. The Board plans to conduct an updated externally facilitated risk review in 2010.

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 Board. The Risk Management Committee carries out an annual review of the business risks. The Board monitors the system of reporting and its effectiveness as a whole and reviews 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. Spirax Sarco Inc. in the USA has successfully completed its business continuity planning exercise.

(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, post-investment review and due diligence requirements where businesses are being acquired. Forward currency contracts are implemented centrally under the control of the Group Treasury Function.

(iii) Operational

All Group companies are required annually 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 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 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 particularly relating to the provision of additional services to the Company 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 59. 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. No significant matters were raised in the reports made in the 11 operating companies 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 and Financial Review on pages 10 to 21. In addition Note 32 on pages 77 to 81 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 March 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 46.