

CORPORATE GOVERNANCE

Combined Code – principles and compliance

This report has been prepared in accordance with Section 1 of the Combined Code on Corporate Governance issued by the Financial Reporting Council in June 2006 (the Combined Code). The report, together with the Remuneration report on pages 49 to 58, describes how the principles set out in the Combined Code have been applied.

The Board is committed to high standards of corporate governance and is pleased to report that throughout the year under review Invensys has been compliant with the provisions of the Combined Code. The Invensys Code of Conduct (which is part of a broader Compliance Programme) aims to ensure the businesses act with integrity and comply with all laws.

The Board

The Board is chaired by Martin Jay, who was appointed non-executive Chairman in July 2003. At 14 May 2008, the Board consisted of two executive directors and four non-executive directors, in addition to the Chairman. Biographies of all directors are presented on pages 10 and 11. Pat Zito was appointed to the Board as a non-executive director on 23 May 2007. The Senior Independent Director is Michael Parker, who has held this role since 7 December 2006. Mr Parker, as Senior Independent Director, is available for shareholders to contact.

Mr Jay has informed the other members of the Board that he is intending to retire as Chairman and a director of the Company at the 2009 Annual General Meeting. By then, he will have been Chairman for six years and believes that it will be an appropriate time to hand over to a successor. He has made his intentions clear now so that the Board can put in place a thorough and orderly process to appoint a new Chairman and ensure that a smooth transfer of responsibilities can take place.

Executive directors are encouraged not to hold more than one external non-executive directorship which is in line with the Combined Code requirement that boards should not agree to full-time executive directors taking on more than one non-executive directorship. Mr Henriksson joined the board of Hexagon AB as a non-executive director on 2 May 2007. In line with the Combined Code requirement, this is the only non-executive directorship that Mr Henriksson holds. Hexagon AB is a Swedish global technology group, listed on the Swedish Stock Exchange, specialising in measurement technologies, polymers and key components.

Prior to giving Mr Henriksson permission to accept this role, the Board undertook a review to ensure there was no conflict between the business of the Group and Hexagon AB.

Board independence

The Board meets the Combined Code requirement that at least half of the Board, excluding the Chairman, should be independent

non-executive directors. The Board considers that all of the non-executive directors are independent for Combined Code purposes.

The Board has a majority of independent non-executive directors and a good balance between non-executive and executive directors, ensuring that no individual or small group dominates the Board's decision making. Terms and conditions of appointment of non-executive directors are available on request from the Company Secretary. Non-executive directors are appointed for an initial three year term from the date of their first election by shareholders until the date of the third Annual General Meeting thereafter. After the initial term, their appointment may be extended for a second term, subject to mutual agreement and shareholder approval.

Division of responsibilities

There is a clear division of responsibilities between the Chairman and the Chief Executive which is defined in writing and approved by the Board. The Chairman is responsible for leadership of the Board and ensuring its effectiveness. He facilitates the contribution of the non-executive directors and ensures constructive relations between the executive and non-executive directors and effective communication with shareholders. The Chief Executive is responsible for executing the strategy approved by the Board and leadership of the Group.

Company Secretary

The Company Secretary is responsible to the Board and advises on all corporate governance matters, ensuring that all Board procedures are followed and that there is a good information flow. To enable the Board to perform its duties, all directors have full and timely access to all relevant information and to the services of the Company Secretary. The Company Secretary is Victoria Hull who was appointed on 1 January 2006 and who acts as secretary to all of the committees of the Board. Ms Hull is also the General Counsel. The appointment and removal of the Company Secretary is decided upon by the Board as a whole.

Meetings

There is an agreed schedule of Board and committee meetings. During the year each of the directors attended such scheduled meetings as set out in the table below. This analysis includes the members' attendance at meetings and does not include attendance of other directors attending at the invitation of the respective committees.

In addition to the scheduled meetings, the Board met on a further 10 occasions, the Remuneration Committee on six occasions, and the Nominating Committee on two occasions. There were also informal meetings of the Chairman and the non-executive directors without the executive directors being present. The Senior Independent Director and non-executive directors also met during the year to appraise the Chairman's performance.

	Board ¹		Audit ¹ Committee		Remuneration ¹ Committee		Nominating ¹ Committee	
	Attended	Possible	Attended	Possible	Attended	Possible	Attended	Possible
Martin Jay	10	10	–	–	6	6	1	1
Ulf Henriksson ²	10	10	–	–	–	–	–	–
Steve Hare	10	10	–	–	–	–	–	–
Bay Green	10	10	6	6	6	6	1	1
Jean-Claude Guez ³	10	10	2	2	6	6	1	1
Michael Parker ²	10	10	6	6	6	6	–	–
Pat Zito ⁴	8	8	5	5	5	5	–	–

¹ Scheduled Board/committee meetings.

² Attendance at Nominating Committee meetings from date of appointment as a member on 6 February 2008.

³ Attendance at Audit Committee meetings until 1 August 2007 when he stepped down as a member.

⁴ Attendance at Board, Audit Committee and Remuneration Committee meetings from his date of appointment to the Company on 23 May 2007.

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Independent financial and professional advice is available to the directors and Board committees, collectively and individually, as circumstances require at the Company's expense.

Role and procedures

There is a formal schedule of matters relating to all major strategic and financial decisions which are reserved for the decision of the Board. During the year, these matters were reviewed against the Institute of Chartered Secretaries and Administrators' model and subsequently updated.

The matters reserved for the Board include approval of the interim results and the formulation of strategic and annual operating plans. In addition, certain decision-making is delegated through structured procedures to committees and, for operational matters, to senior management. Although all the directors have an equal responsibility for the operations of Invensys, the role of the non-executive directors is particularly important in ensuring that the strategy and business proposals of the executive management team are fully discussed and examined to ensure that they meet the long-term interests of shareholders and also take account of issues affecting employees, customers, suppliers and the many communities within which Invensys conducts its business. At least one full day's meeting every year is devoted to the overall strategic planning of the Group. The Board delegates specific authorities to its Nominating Committee, Audit Committee and Remuneration Committee. Reports of these committees are set out on pages 46 to 58. All directors receive copies of all committee minutes and the chairman of each committee provides an update on matters of significance at the Board meeting following the committee meeting.

Board and committees: performance evaluation

The Board has a formal review process with discrete components covering the evaluation of the Board's collective performance, the appraisal of the performance of individual directors, including the Chairman, and each of the Board's committees.

Evaluation of executive directors is conducted by the Chairman and non-executive directors. Appraisal of the non-executive directors is led by the Chairman in consultation with all directors. Additionally, each non-executive director is asked to assess themselves. The evaluation of the Chairman is led by the Senior Independent Director in consultation with the other non-executive directors, taking into account the views of the executive directors. Individual feedback is provided by the Chairman to each of the non-executive directors and by the Senior Independent Director to the Chairman.

In relation to the evaluation of the Board and its committees, an internal questionnaire based on the Combined Code provisions is used for this process. The evaluation process involves assessment by reference to the relevant roles and responsibilities under review, the current terms of reference of the committees and best practice. The results of the evaluation provide the basis for continuous improvement in the Board's procedures and the Board's action plans and objectives for the following year.

The Board remains satisfied that each ongoing director remains committed to his role and that the Board and each of its committees remains effective.

Induction and development

On appointment, new directors receive an induction programme tailored to their experience, including an induction pack comprising relevant information, scheduled meetings with key personnel and advisers and site visits. As part of his induction, Mr Zito, who was appointed as a non-executive director on 23 May

2007, met senior corporate and business leaders and advisers of the Group. The continuing development of directors, collectively and individually, is mainly effected through the provision to them by relevant external and internal advisers of briefings on matters of current significance to the Group and also through attendance at external briefings. During the year directors received regular updates on legislative developments (e.g. the Companies Act 2006 and the Corporate Manslaughter and Corporate Homicide Act 2007) and other matters of legal significance. A pensions training session was also organised, which all directors attended. The Board ensures that directors have access to independent professional advice on how to discharge their responsibilities as directors of the Company.

Communication with shareholders

Communication with shareholders is at all times given a high priority and a number of means are used to promote greater understanding and dialogue with investment audiences. In order to develop an understanding of the views of major shareholders, the Board receives regular reports from the Chief Executive and the Group's investor relations team. The Chairman and the Senior Independent Director are available to meet with major shareholders on request.

As explained in the Chairman's statement, the Board has decided to cease full quarterly reporting following the redemption of the remaining High Yield Bonds in March 2008. Shareholders will however be kept informed of the progress of the Group during the course of a year through half year and full year results, interim management statements and other announcements of significant developments that are released through the London Stock Exchange and other news services. The Chief Executive and Chief Financial Officer maintain regular dialogue with institutional shareholders and participate in sector conferences. Shareholders can also raise questions directly with the Company at any time by contacting the investor relations team, whose contact details are listed on the Group's website.

Additionally, directors are available at the Annual General Meeting for shareholders' questions. The Annual report and accounts are made available to shareholders at least 20 working days prior to the Annual General Meeting. Voting on resolutions proposed separately is conducted by polls at general meetings and voting results are announced through the London Stock Exchange and other news services; the results and proxy levels are available on the website and on request. At the last Annual General Meeting, the Company's Articles of Association were amended to permit the Company to send or supply communications to shareholders electronically and the Company now supplies information such as notices of meetings, forms of proxy and the annual report via the website. Shareholders will be notified by email or post when new information is available on the website. The Company will continue to send hard copy communications to those shareholders who have requested to receive communications in hard copy form. Shareholders may at any time revoke a previous instruction in order to receive hard copies or electronic copies of shareholder information.

Nominating Committee report Membership

The Nominating Committee currently comprises the Chairman (who chairs the Nominating Committee), the Chief Executive and three independent non-executive directors. The table below details members of the Nominating Committee during the year under review:

Name	Date of appointment
Current members	
Martin Jay	January 2003, Chairman of the Nominating Committee since 23 July 2003
Bay Green	1 January 2005
Jean-Claude Guez	23 July 2003
Ulf Henriksson	6 February 2008
Michael Parker	6 February 2008

Role

The current terms of reference for the Nominating Committee are available on the Group's website.

The Nominating Committee's responsibilities include:

- making recommendations to the Board for the appointment, reappointment and retirement of directors;
- reviewing the performance of directors;
- reviewing the composition and size of the Board and its committees;
- setting the procedure for the appointment of new directors to the Board; and
- succession planning.

Meetings

The Nominating Committee held one scheduled meeting and two unscheduled meetings during the year under review. Attendance at the scheduled meeting is shown in the table on page 45. At the request of the Nominating Committee, the Chief Executive (prior to his appointment as a member) and Chief Financial Officer were invited to attend some meetings of the Committee.

Principal matters considered during the year under review included the evaluation of those directors proposed for election or re-election at the Annual General Meeting (with no individual director participating in any matter relating to himself) and Board succession planning.

All directors are required to retire by rotation no later than the third Annual General Meeting following their appointment or reappointment. No director is proposed for election for a further term of three years unless the Nominating Committee has, following evaluation, recommended such reappointment to the Board. The recommendation of the Nominating Committee on the re-election of Bay Green as a director is described in the Notice of Annual General Meeting. The terms and conditions of appointment of non-executive directors are available on request from the Company Secretary.

Audit Committee report

Membership

The Audit Committee currently comprises three independent non-executive directors. Details regarding members of the Audit Committee during the year under review are set out below:

Name	Date of appointment
Current members	
Bay Green	Acting Chairman of the Audit Committee from 3 August 2006 and appointed permanent Chairman from 7 December 2006
Michael Parker	2 August 2006
Pat Zito	23 May 2007

Jean-Claude Guez served on the Audit Committee from 20 September 2006 until 1 August 2007.

Mr Green is a qualified chartered accountant and fellow of the Institute of Chartered Accountants of England and Wales and, with over 30 years in financial roles, he is considered to have recent and relevant financial experience for the purposes of the Combined Code. He has held a number of senior positions in Dresdner Kleinwort and is a specialist adviser to the Wholesale and Institutional Markets Business Unit of the Financial Services Authority.

Role

The Audit Committee is appointed by the Board from the non-executive directors of the Company. The current terms of reference for the Audit Committee are available on the Group's website.

The Audit Committee's responsibilities include:

- monitoring the integrity of the Group's financial statements and reviewing significant financial reporting issues and accounting policies;
- reviewing the Group's systems of internal control and risk management;
- reviewing the effectiveness of the internal audit function;
- making recommendations to the Board on the appointment, dismissal, remuneration and terms of engagement of external auditors;
- reviewing the external auditors' qualification, expertise, resources, independence and effectiveness, taking into account professional and regulatory requirements;
- implementing policies on the engagement of external auditors to supply non-audit services; and
- reporting to the Board any matters where it considers improvement is needed and making recommendation as to the steps to be taken.

Meetings

The Audit Committee held six scheduled meetings during the year under review. There were no unscheduled meetings. Attendance is shown in the table on page 45. At least once a year, the Audit Committee and external auditors meet without management present. At the invitation of the Audit Committee, all directors who are not members normally attend all meetings. In addition, other senior managers are invited as required.

Principal matters considered during the year under review included:

- review of the financial disclosures in the Group's Annual report and accounts, half-yearly financial report and quarterly financial results;
- review of the effectiveness of the internal audit function, consideration of internal audit reports and the annual internal audit programme;
- review of the effectiveness of the Group's internal controls and risk management processes and procedures;
- approval of the external audit plan and fee proposal;
- the policy on auditor independence and provision of audit and non-audit services by the auditor;
- the assessment of the effectiveness of the external auditors;
- recommendation to the Board of the reappointment of Ernst & Young LLP as the external auditor; and
- monitoring, through the Risk Committee, the Group's whistle-blowing programme.

The Audit Committee has guidelines to ensure that the independence of Ernst & Young LLP, as the auditor of the Group's financial statements, is not impaired by providing non-audit services. These guidelines govern the provision of non-audit services by Ernst & Young LLP by identifying certain non-audit services that

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the auditor is prohibited from providing. Permitted categories of non-audit services are defined and approved by the Chairman of the Audit Committee. The engagements for non-audit services are subject to formal approval based on the level of fees involved. The Audit Committee has agreed a pre-approval process whereby certain non-audit services up to an agreed value can be provided. Such services are subsequently reported to the Audit Committee. Details of the amounts paid to Ernst & Young LLP as external auditor during the year for audit and other services are set out in Note 5 to the Group financial statements.

Remuneration Committee report

Details of the Remuneration Committee and its policies, together with information on the remuneration and share interests of directors, is set out in the Remuneration report on pages 49 to 58.

Internal control

The Board has ultimate responsibility for the system of internal control and for reviewing its effectiveness. Each of the Group's businesses is individually accountable to the Chief Executive and is managed by a president who, with his senior management team, provides day-to-day control over the business' operations within the strategic guidelines and delegated authorities determined by the Board. The internal control system is designed to meet the Group's particular needs and the risks to which it is exposed, but it should be appreciated that, however effective a system of internal control is, it can provide only reasonable and not absolute assurance against material misstatement or loss.

The Board has established a structured approach to risk management with the processes to identify and manage key risks facing the Group being an integral part of the control environment. The Risk Committee reports to the Board through the Audit Committee. The Risk Committee is responsible for the system of risk management and for the reporting of key risks and the associated mitigating management actions. The Risk Committee includes the Head of Business Risk (Chairman of the Risk Committee since 6 March 2007), the Chief Financial Officer, the Chief Executive, the General Counsel and Company Secretary, the Group Financial Controller, the VP Tax and Treasury, the SVP Environmental, Health, Safety and Sustainability and the VP Risk Management and Insurance. During the year, its activities have included reviewing the Group's risk framework and its monitoring processes. A summary of the principal risks facing the Group is presented on pages 42 to 44.

In accordance with the Turnbull guidance, the Board confirms that it has undertaken its annual assessment of the Group's system of internal control. Inputs into the assessment undertaken by the Audit Committee included:

- consideration of the key risks facing the businesses as part of the review of the Group's strategic planning and annual operating planning processes;
- review of the enhancements to the overall control environment;
- consideration of the key elements of the Group's control processes including organisational structure, the application of governance rules and systems, information management including monthly reporting routines and risk management activities;
- reports received from both internal and external audit during the course of the year; and
- the findings from the annual self-assessment questionnaire which requires all senior managers, from reporting unit level upwards, to certify compliance with the Group's financial and operational procedures and controls, including environmental, health and safety matters and the Invensys Code of Conduct.

Following detailed review, the Audit Committee reported on its findings to the Board. The Board is satisfied that the information that it has received throughout the year and for its annual review together with the procedural review framework that has been established are sufficient to enable it to review the effectiveness of the Group's system of internal control. Whilst areas for improvement in control have been identified and actions initiated on account of the above processes, no significant shortcomings in internal control were identified as a result of the annual assessment. The internal control process has been in place for the year under review and up to the date of approval of the Annual report and accounts.

Internal audit

Internal audit has a direct reporting line to the Chairman of the Audit Committee and its responsibilities include the examination and evaluation of the scope and effectiveness of the Group's system of internal control. The audit plan is constructed to provide geographic coverage over broadly a three year cycle with a degree of tailoring to address specific risk concerns. During the year, it reported regularly to the Audit Committee on its assessment of internal control issues arising in the course of its internal audit reviews of the Group's operations. Each year a consolidated review is provided to assist the Board to undertake its own annual review of internal control.

Historically the internal audit plan has been discharged by a team of in-house auditors. Having regard to the changing nature of the Group's business, the geographic spread of operators and the need for certain specialist audit resources (e.g. IT), the decision was taken to outsource the majority of internal audit work to Deloitte & Touche LLP. The transition was largely completed by the end of April 2008. A small function, reporting to the Head of Business Risk, has been retained to manage the outsourcing contract and undertake certain ad hoc assignments.

Whistle-blowing

The Audit Committee reviews the Group's arrangements under which staff can, on a confidential basis, raise concerns about potential irregularities and arrangements for follow-up actions. A helpline is operated by Global Compliance Services Inc., an independent company, and is publicised to employees via the Invensys Code of Conduct. Any investigations are undertaken by the Company Secretary, or at her direction, and any material investigations are brought to the immediate attention of the Audit Committee which determines an appropriate follow-up action. Statistics on the volume and general nature of calls are reported annually to the Audit Committee and the Board. In addition, staff raise concerns through other means such as email or letter sent to the Board or management, which correspondence is investigated in the same manner as concerns raised through the helpline. No material issues were reported through these processes during the year.