

CORPORATE GOVERNANCE

Statement of Compliance with the Combined Code

The company has applied all of the principles set out in section 1 of the Combined Code on Corporate Governance (the Code) relating to the structure and composition of the board, the remuneration of the directors, relations with shareholders and procedures for financial reporting, internal control and audit. This statement describes how the principles of the Code have been applied.

Throughout the year, the group has been in compliance with the provisions of the Code with the exception of the matter noted on page 31.

Directors and the Board

The board is responsible to the company's shareholders for the group's system of corporate governance, its strategic objectives and the stewardship of the company's resources and is ultimately responsible for social, environmental and ethical matters. The board meets at least seven times per year and delegates specific responsibilities to board committees, as described below. The board reviews the key activities of the business, and receives papers and presentations to enable it to do so effectively. The Company Secretary is responsible to the board and is available to individual directors in respect of board procedures.

The board comprises the Chairman, the Chief Executive, three other executive directors and six other independent non-executive directors. Mr H R Jenkins was Senior Independent Director throughout the period. Mr C D Mackay will take over as Senior Independent Director on 16th July 2003 following Mr Jenkins' retirement from the board. The role of non-executive directors is to enhance independence and objectivity of the board's deliberations and decisions. The executive directors have specific responsibilities, which are detailed on page 27, and have direct responsibility for all operations and activities.

All directors submit themselves for re-election every three years.

Committees of the Board

The Chief Executive's Committee is responsible for the recommendation to the board of strategic and operating plans and on decisions reserved to the board where appropriate. It is also responsible for the executive management of the group's business. The Committee is chaired by the Chief Executive and meets monthly. It comprises the executive directors and six senior executives of the company.

The Audit Committee is a sub-committee of the board whose purpose is to assist the board in the effective discharge of its responsibilities for financial reporting and corporate control. The Committee meets twice a year and has been chaired by Mr H R Jenkins. Mr A M Thomson will take over as Chairman of the Audit Committee following Mr Jenkins' retirement. It comprises all the non-executive directors with the Chief Executive, the Group Finance Director and the external and internal auditors in attendance.

The Nominations Committee is a sub-committee of the board responsible for advising the board and making recommendations on the appointment of new directors. The Committee is chaired by Mr H M P Miles and comprises all the non-executive directors.

The Management Development and Remuneration Committee (MDRC) is a sub-committee of the board, which determines on behalf of the board the remuneration of the executive directors. Since 25th March 2003 the Committee has been chaired by Mr C D Mackay and comprises all the non-executive directors. The Chief Executive and Director of Human Resources attend by invitation except when their own performance and remuneration are discussed.

Directors' Remuneration

The Remuneration Report on pages 32 to 37 includes details of remuneration policies and of the remuneration of the directors.

Relations with Shareholders

The board considers effective communication with shareholders, whether institutional investors, private or employee shareholders, to be extremely important.

The company reports formally to shareholders twice a year, when its half year and full year results are announced and an interim report and a full report are issued to shareholders. These reports are posted on Johnson Matthey's website (www.matthey.com). At the same time, executive directors give presentations on the results to institutional investors, analysts and the media in London and other international centres. Copies of major presentations are also posted on the company's website.

The Annual General Meeting (AGM) of the company takes place in London and formal notification is sent to shareholders with the annual report at least 20 working days in advance of the meeting. The directors are available, formally during the AGM and informally afterwards, for questions. Details of the 2003 AGM are set out in the notice of the meeting enclosed with this annual report.

Accountability, Audit and Control

The statement of directors' responsibilities in relation to the accounts is set out on page 38.

In its reporting to shareholders, the board aims to present a balanced and understandable assessment of the group's financial position and prospects.

The group's organisational structure is focused on its four divisions. These entities are all separately managed, but report to the board through a board director. The executive management team receive monthly summaries of financial results from each division through a standardised reporting process.

The group has in place a comprehensive annual budgeting process including forecasts for the next two years. Variances from budget are closely monitored.

The board has overall responsibility for the group's system of internal controls and for reviewing its effectiveness. The internal control systems are designed to meet the group's needs and address the risks to which it is exposed. Such a system can provide reasonable but not absolute assurance against material misstatement or loss.

CORPORATE GOVERNANCE

There is a continuous process for identifying, evaluating and managing the significant risks faced by the company which has been in place during the year under review and up to the date of approval of the annual report and accounts. The board regularly reviews this process.

The assessment of group and strategic risks is reviewed by the board and updated on an annual basis. At the business level, the processes to identify and manage the key risks are an integral part of the control environment. Key risks and internal controls are the subject of regular reporting to the Chief Executive's Committee.

The Group Control Manual, which is distributed to all group operations, clearly sets out the composition, responsibilities and authority limits of the various board and executive committees and also specifies what may be decided without central approval. It is supplemented by other specialist policy and procedures manuals issued by the group, divisions and individual business units or departments. The high intrinsic value of many of the metals with which the group is associated necessitates stringent physical controls over precious metals held at the group's sites.

The internal audit function is responsible for monitoring the group's systems of internal financial controls and the control of the integrity of the financial information reported to the board. The Audit Committee approves the plans for internal audit reviews and receives the reports produced by the internal audit function on a regular basis. Actions are agreed with management in response to the internal audit reports produced.

In addition, significant business units provide assurance on the maintenance of financial and non-financial controls and compliance with group policies. These assessments are summarised by the internal audit function and a report is made annually to the Audit Committee.

The directors confirm that the system of internal control for the year ended 31st March 2003 and the period up to 31st May 2003 has been established in accordance with the guidance "Internal Control: Guidance for Directors on the Combined Code" issued in September 1999 and that they have reviewed the effectiveness of the system of internal control.

Auditors

The performance of the auditors is reviewed by the Audit Committee on a regular basis, including a formal review of the external auditors every three years.

Both the board and the external auditors (KPMG Audit Plc) have for many years had safeguards to avoid the possibility that the auditors' objectivity and independence could be compromised. Our policy in respect of services provided by the external auditors is as follows:

- Audit related services – the external auditors are invited to provide services which, in their position as auditors, they must or are best placed to undertake. It includes formalities relating to borrowings, shareholders and other circulars, various other regulatory reports and work in respect of acquisitions and disposals.
- Tax consulting – in cases where they are best suited, we use the external auditors. All other significant tax consulting work is put out to tender.
- General consulting – in recognition of public concern over the effect of consulting services on auditors' independence, our policy is that the external auditors are not invited to tender for general consulting work.

Non-Compliance with the Combined Code

The item in the Code with which the group did not comply in full throughout the period together with the appropriate Code reference is stated below:

Two of the executive directors were employed on contracts subject to two years' notice at any time, which the MDRC previously considered appropriate in the overall context of the executive directors' terms of employment. The notice period in these service contracts has now been reduced, without compensation, to twelve months. (B.1.7)

Corporate Social Responsibility

Measures to ensure ethical conduct and the identification and assessment of risks associated with social and environmental matters are managed in conjunction with all other business risks and reviewed at regular meetings of the board and the Chief Executive's Committee.

A summary report on the group's policies and targets for corporate social responsibility is set out on pages 22 to 25. A full version of the report is available on the company's website.

Environmental risks are identified and assessed by the Environment, Health and Safety Committee (EHSC), which meets every two months. This is chaired by the Director of Environment, Health and Safety (EHS) and reports to the Chief Executive's Committee. All divisional directors are members of the EHSC.

Performance is monitored using monthly statistics and detailed site audit reports. The Audit Committee considers risks associated with EHS and monitors performance through the annual control self-assessment process conducted by the internal audit function.

Risks from employment and people issues are identified and assessed by the Executive Development Committee, which meets every two months. This is chaired by the Chief Executive and is attended by all divisional directors and the Director of Human Resources.

Employment contracts, handbooks and policies specify acceptable business practices and the group's position on ethical issues. The Group Control Manual and security manuals provide further operational guidelines to reinforce these.

Going Concern

The directors have a reasonable expectation that the group has sufficient resources to continue in operational existence for the foreseeable future and have, therefore, adopted the going concern basis in preparing the accounts.