

Directors' report

This is the Directors' report of 3i Group plc for the year to 31 March 2006 ("the year").

Principal activity 3i Group plc is a world leader in private equity and venture capital. The principal activity of the Company and its subsidiaries ("the Group") is investment. It invests in a wide range of growing independent businesses. Its objective is to maximise shareholder value through growth in total return.

Tax and investment company status The Company is an investment company as defined by section 266 of the Companies Act 1985 and carries on business as an investment trust.

HM Revenue & Customs has approved the Company as an investment trust under section 842 of the Income and Corporation Taxes Act 1988 for the financial period to 31 March 2005. Since that date the Company has directed its affairs to enable it to continue to be so approved.

Regulation The Company was authorised and regulated by the Financial Services Authority ("FSA") until 27 May 2005, when it relinquished its deposit taking status. 3i Investments plc, a wholly owned subsidiary of the Company, is authorised and regulated by the FSA under the Financial Services and Markets Act 2000. Where applicable, certain Group subsidiaries' businesses outside the United Kingdom are regulated locally by relevant authorities.

Results and dividends The financial statements of the Company and the Group for the year to 31 March 2006 appear on pages 61 to 88.

Total recognised income and expense for the year was £831 million (2005: £501 million, as restated for IFRS). As part of the arrangements approved by shareholders to return value to shareholders, a special dividend of 40.7p per share was paid on 22 July 2005 in respect of the year to 31 March 2006. A further interim dividend of 5.5p per share in respect of that year was paid on 4 January 2006. The Directors recommend a final dividend of 9.7p per share be paid in respect of the year to 31 March 2006 to shareholders on the register at the close of business on 23 June 2006.

By a deed of waiver dated 9 June 1994, Mourant & Co. Trustees Limited in its capacity as trustee of The 3i Group Employee Trust ("the Employee Trust") waived (subject to certain minor exceptions) all dividends declared by the Company after 26 May 1994 in respect of shares from time to time held by the Employee Trust (currently 11,311,280 shares).

Operations The Group operates through a network of offices in Europe, Asia and the US. The Group also manages a number of funds established with major institutions and pension funds to make equity and equity-related investments in unquoted businesses in Europe and Asia.

Management arrangements 3i Investments plc acts as investment manager to the Company and certain of its subsidiaries. Contracts for these investment management and other services, for which regulatory authorisation is required, provide for fees based on the work done and costs incurred in providing such services. These contracts may be terminated by either party on reasonable notice.

3i plc provides the Group with certain corporate and administrative services, for which no regulatory authorisation is required, under contracts which provide for fees based on the work done and costs incurred in providing such services. The administrative services contract between 3i plc and 3i Investments plc may be terminated by either party on three months' notice. The administrative services contracts between 3i plc and other Group companies may be terminated by either party on reasonable notice.

Business review The Chairman's statement on pages 4 and 5, the Chief Executive's statement on pages 6 and 7, the "Our vision" section on pages 8 to 11 and the Business review on pages 12 to 35 report on the Group's development during the year to 31 March 2006, its position at that date and the Group's likely future development. Information fulfilling the requirements of the Business Review can be found in the Business review on pages 12 to 35 and in the Corporate responsibility section on pages 36 to 41, which are incorporated in this report by reference.

Share capital

Pre-consolidation share capital movements The issued share capital of the Company as at 1 April 2005 was 614,409,167 ordinary shares of 50p each. This increased by 268,792 shares to 614,677,959 ordinary shares of 50p each in the period from 1 April 2005 to 10 July 2005 on the issue of shares to the trustee of The 3i Group Share Incentive Plan and on the exercise of options under the Group's executive share option plans and The 3i Group Sharesave Scheme.

Consolidation of share capital Pursuant to resolutions passed at an Extraordinary General Meeting ("EGM") of the Company, on 11 July 2005 the issued share capital of the Company, of 614,677,959 ordinary shares of 50p each, was consolidated into 578,520,432 ordinary shares of 53½p each.

Post-consolidation share capital movements At the EGM in July 2005, the Directors were authorised to repurchase up to 57,800,000 shares of 53½p each in the Company (representing approximately 10% of the Company's issued share capital as at 10 May 2005) until the Company's Annual General Meeting in 2006 or 5 October 2006, if earlier. The Board indicated that it would only use this authority to repurchase Company shares with an aggregate value of approximately £250 million. In the year to 31 March 2006, the Company cancelled 30,186,896 ordinary shares of 53½p each which had been purchased pursuant to this authority.

In the period from 11 July 2005 to 31 March 2006, a total of 2,222,966 ordinary shares of 53½p were issued (to the trustee of The 3i Group Share Incentive Plan and on the exercise of options under the Group's executive share option plans and The 3i Group Sharesave Scheme).

Accordingly, between 11 July 2005 and 31 March 2006, the consolidated share capital of the Company decreased by 27,963,930 ordinary shares to 550,556,502 ordinary shares of 53½p each.

Major interests in shares As at 3 May 2006, the Company had been notified of the following interests in the Company's shares in accordance with sections 198 to 208 of the Companies Act 1985.

	%	Number of shares
Prudential plc and subsidiary companies	6.14	34,716,123
FMR Corporation and Fidelity International Limited and their subsidiary companies	4.95	27,255,702
Legal & General Group	3.85	21,844,391

Directors' interests Details of the Directors' interests in the Company's shares are shown in note 39 to the financial statements on page 88. Save as shown in note 39, no Director had any disclosable interest in the shares, debentures or loan stock of the Company or in the shares, debentures or loan stock of its subsidiaries during the period and there have been no changes in the above interests between 1 April 2006 and 3 May 2006.

Corporate governance Throughout the year, the Company complied with the provisions of section 1 of the Combined Code on corporate governance published by the Financial Reporting Council in July 2003.

The Company's approach to corporate governance The Company has a policy of seeking to comply with established best practice in the field of corporate governance. The Board has adopted core values and Group standards which set out the behaviour expected of staff in their dealings with shareholders, customers, colleagues, suppliers and other stakeholders of the Company. One of the core values communicated within the Group is a belief that the highest standard of integrity is essential in business.

The Board's responsibilities and processes The Board is responsible to shareholders for the overall management of the Group. It determines matters including financial strategy and planning and takes major business decisions. The Board has put in place an organisational structure. This is further described under the heading "internal control". The Board has approved a formal schedule of matters reserved to it and its duly authorised Committees for decision. These include:

- approval of the Group's overall strategy, strategic plan and annual operating budget;
- approval of the Company's interim and annual financial statements and changes in the Group's accounting policies or practices;
- changes relating to the capital structure of the Company or its regulated status;
- major capital projects;
- major changes in the nature of business operations;
- investments and divestments in the ordinary course of business above certain limits set by the Board from time to time;
- adequacy of internal control systems;
- appointments to the Board and Management Committee;
- principal terms and conditions of employment of members of Management Committee; and
- changes in employee share schemes and other long-term incentive schemes.

Matters delegated to management include implementation of the Board approved strategy, day-to-day operation of the business, the appointment of all executives below Management Committee and the formulation and execution of risk management policies and practices.

A Group succession and contingency plan is prepared by management and reviewed periodically by the Board. The purpose of this plan is to identify suitable candidates for succession to key senior management positions, agree their training and development needs, and ensure the necessary human resources are in place for the Company to meet its objectives.

During the year, the principal matters considered by the Board included:

- the Group strategic plan, budget and financial resources;
- the Group's capital structure, balance sheet efficiency and the return of capital to shareholders;
- regular reports from the Chief Executive;
- the recommendations of the Valuations Committee on valuations of investments;
- the Company's share price performance and findings from a shareholder perception study;
- organisational capability, succession planning and findings from a staff survey;
- the establishment of a European Commercial Paper programme;
- establishing a further European Buyout Fund;
- risk management;
- requirements for operating and financial reviews and key performance indicators;
- independence of non-executive Directors; and
- funding of the 3i Group Pension Plan.

Information Reports and papers are circulated to the Directors in a timely manner in preparation for Board and Committee meetings. These papers are supplemented by information specifically requested by the Directors from time to time.

During the year, there were six meetings of the Board of Directors. The Directors who served throughout the year attended all six meetings save for Mr O H J Stocken who attended five meetings. Mr R W Perry attended the one meeting held before his retirement as a Director on 6 July 2005.

Performance evaluation During the year, the Board conducted its annual review of performance of the Board as a whole and of individual contributions. The Chairman led the process with the aid of the Board's external consultant. All Board members completed a questionnaire and gave personal views to the Chairman, who also sought views from all members of the Management Committee. The Chairman gave feedback to the Board and to individual Directors. The Senior Independent Director conducted a parallel process to review the performance of the Chairman. These processes also involved evaluation by members of Board Committees of their performance.

The Board concluded that the changes that had been made in the schedule to allow for more strategic discussion had been beneficial and should be continued, including the introduction of a second awayday during the year. Having reviewed the remit and functioning of Committees, the Board decided to continue to maintain the existence of the Valuations Committee, as well as the Audit and Compliance Committee, in order to provide a twice-yearly opportunity to focus on valuation methodology and judgments in advance of the audit of results. The average size of the Company's investments had risen, and changes in the valuation guidelines published by the British Venture Capital Association required a more tailored approach. The Board and the Audit and Compliance Committee also reviewed the functions and membership of the management Risk Committee and supported the broadening of its remit. The Remuneration Committee reviewed policy and decided to consult major shareholders on developments designed to align the Company's systems more closely with the private equity industry and to clarify the framework for share-based awards. Directors concluded that the extra Board time that had been given to consideration of human resource management, career development and succession planning was extremely valuable and should be continued. The Board decided to continue the practice of holding at least one meeting a year away from the Company's head office, in order to enable members to spend time with the executives responsible for building the Company's global capability. It was also decided to continue the process of adding external capability to the Board to match changes in the business and in financial markets.

The roles of the Chairman and the Chief Executive The division of responsibilities between the Chairman of the Board and the Chief Executive is clearly defined and has been approved by the Board.

The Chairman The Chairman leads the Board in the determination of its strategy and in the achievement of its objectives. The Chairman is responsible for organising the business of the Board, ensuring its effectiveness and setting its agenda. The Chairman has no involvement in the day-to-day business of the Group. The Chairman facilitates the effective contribution of non-executive Directors and constructive relations between executive and non-executive Directors. The Chairman ensures that regular reports from the Company's brokers are circulated to the non-executive Directors to enable non-executive Directors to remain aware of shareholders' views. The Chairman ensures effective communication with the Company's shareholders.

The Chief Executive The Chief Executive has direct charge of the Group on a day-to-day basis and is accountable to the Board for the financial and operational performance of the Group. The Chief Executive has formed a committee called Management Committee to enable him to carry out the responsibilities delegated to him by the Board. The Committee comprises the executive Directors, the Company Secretary, Ms D R Collis, Mr C P Rowlands, Mr J B C Russell, Mr A J M Taylor and Mr P Waller. The Committee meets on a regular basis to consider operational matters and the implementation of the Group's strategy.

Senior Independent Director The Board has appointed Mr O H J Stocken as Senior Independent Director, to whom, in accordance with the Combined Code, concerns can be conveyed.

Directors The Board comprises the Chairman, six other independent non-executive Directors and three executive Directors. Biographical details for each of the Directors are set out on pages 42 and 43. Baroness Hogg (Chairman), Mr O H J Stocken, Mr P E Yea, Mr S P Ball, Dr P Mihatsch, Mme C J M Morin-Postel, Mr M J Queen, Mr F D Rosenkranz, Sir Robert Smith and Mr F G Steingraber served throughout the period under review. Mr R W Perry served as a Director until 6 July 2005.

In addition to fulfilling their legal responsibilities as Directors, non-executive Directors are expected to bring an independent judgment to bear on issues of strategy, performance, resources and standards of conduct, and to help the Board provide the Company with effective leadership. They are also expected to ensure high standards of financial probity on the part of the Company and to monitor the effectiveness of the executive Directors.

The Board's discussions, and its approval of the Group's strategic plan and annual budget, provide the non-executive Directors with the opportunity to contribute to and validate management's plans and assist in the development of strategy. The non-executive Directors receive regular management accounts, reports and information which enable them to scrutinise the Company's and management's performance against agreed objectives.

Directors' independence All the non-executive Directors, including the Chairman, are considered by the Board to be independent for the purposes of the Combined Code. The Board assesses and reviews the independence of each of the non-executive Directors at least annually having regard to the potential relevance and materiality of a Director's interests and relationships rather than applying rigid criteria in a mechanistic manner. The Board has considered Mr O H J Stocken and Mme C J M Morin-Postel's common non-executive directorship of Pilkington plc and concluded that it did not affect their independence. The Board has also considered Dr P Mihatsch's non-executive directorships within the Vodafone Group plc group of companies and Mr P E Yea's non-executive directorship of Vodafone Group plc and concluded that this did not affect Dr P Mihatsch's independence.

No Director was materially interested in any contract or arrangement subsisting during or at the end of the financial period that was significant in relation to the business of the Company.

Directors' service contracts Details of Directors' employment contracts are set out in the Directors' remuneration report on page 58.

Training and development The Company has developed a training policy which provides a framework within which training for Directors is planned with the objective of ensuring Directors understand the duties and responsibilities of being a Director of a listed company. All Directors are required to update their skills and maintain their familiarity with the Company and its business continually. Presentations on different aspects of the Company's business are made regularly to the Board. On appointment, all non-executive Directors have discussions with the Chairman and the Chief Executive following which appropriate briefings on the responsibilities of Directors, the Company's business and the Company's procedures are arranged. The Company provides opportunities for non-executive Directors to obtain a thorough understanding of the Company's business by meeting members of the senior management team who in turn arrange, as required, visits to investment offices and support departments.

During the year the Directors received training on Directors' responsibilities for the operating and financial review, the new Listing Rules, the Market Abuse Regime and the Company Law Reform Bill. In addition, the non-executive Directors received presentations on the Company's Nordic investment business and on technology investment.

The Company has procedures for Directors to take independent legal or other professional advice about the performance of their duties.

Re-election Subject to the Company's Articles of Association, the Companies Acts and satisfactory performance evaluation, non-executive Directors are appointed for an initial period of three years. Before the third and sixth anniversaries of a non-executive Director's first appointment, the Director discusses with the Board whether it is appropriate for a further three year term to be served. The reappointment of non-executive Directors who have served for more than nine years is subject to annual review.

The Company's Articles of Association provide for:

- a) Directors to retire at the first Annual General Meeting ("AGM") after their appointment by the Board and for the number nearest to, but not exceeding, one-third of the remaining Directors to retire by rotation at each AGM;
- b) all Directors to retire at least every three years; and
- c) any Director aged 70 or over at the date of the AGM to retire.

Subject to the Articles of Association, retiring Directors are eligible for reappointment.

In accordance with the Articles of Association, at the AGM to be held on 12 July 2006, Mme C J M Morin-Postel, Mr M J Queen and Mr F D Rosenkranz will retire by rotation and, being eligible, offer themselves for reappointment. The Board's recommendation for the reappointment of Directors is set out in the Notice of AGM.

Directors' indemnities The Company's Articles of Association provide that, subject to the provisions of the Companies Acts, the Directors shall be indemnified against liabilities incurred by them as Directors in defending any proceedings in which judgment is given in their favour, or where they have been acquitted or been granted relief by the court. Pursuant to the Companies (Audit, Investigations and Community Enterprise) Act 2004 and the Company's Articles of Association, during the year the Company put in place Qualifying Third Party Indemnity Provisions (as defined under section 309B of the Companies Act 1985) for the benefit of the Company's Directors and the Company Secretary. These provisions remain in force.

Under the rules of the 3i Group Pension Plan ("the Plan"), the Company has granted an indemnity to the directors of Gardens Pension Trustees Limited (a corporate trustee of the Plan and a wholly owned subsidiary of the Company) against liabilities incurred as directors of that corporate trustee.

The Board's committees The Board is assisted by various standing committees of the Board which report regularly to the Board. The membership of these committees is regularly reviewed by the Board. When considering committee membership and chairmanship, the Board aims to ensure that undue reliance is not placed on particular Directors.

These committees all have clearly defined terms of reference which are available at www.3igroup.com. The terms of reference of the Audit and Compliance Committee, the Remuneration Committee and the Nominations Committee provide that no one other than the particular Committee chairman and members may attend a meeting unless invited to attend by the Committee.

Audit and Compliance Committee The Audit and Compliance Committee comprises Mr O H J Stocken (Chairman), Mme C J M Morin-Postel, Mr F D Rosenkranz and Sir Robert Smith, all of whom served throughout the period. All the members of the Committee are independent non-executive Directors. The Board is satisfied that the Committee Chairman, Mr O H J Stocken, has recent and relevant financial experience. During the year, there were five meetings of the Committee all of which were attended by all members of the Committee save for one meeting which was not attended by Mme C J M Morin-Postel.

During the year, the Committee:

- reviewed the effectiveness of the internal control environment of the Group and the Group's compliance with its regulatory requirements and received reports on bank covenants, third party liabilities and off-balance sheet liabilities;
- reviewed and recommended to the Board the accounting disclosures comprised in the interim and annual financial statements of the Company and reviewed the scope of the annual audit plan and the audit findings;
- reviewed matters relating to the Group's key performance indicators, the introduction of International Financial Reporting Standards and proposals for operating and financial reviews and enhanced business reviews;
- received regular reports from the internal audit function, monitored its activities and effectiveness, and agreed the annual internal audit plan;
- received regular reports from the regulatory compliance function and Risk Committee, and monitored their activities and effectiveness;
- oversaw the Company's relations with its external auditors including assessing auditor performance and independence, recommending the auditors' reappointment and approving the auditors' fees;
- met with the external auditors and the heads of the internal audit and compliance functions individually, all in the absence of management;
- reviewed the Company's "whistle blowing" policy to ensure that arrangements were in place for staff to raise, in confidence, matters of concern; and
- considered whether matters existed which could give rise to conflicts of interests between Directors and the Company.

Remuneration Committee The Remuneration Committee comprises Mr F D Rosenkranz (Chairman), Mme C J M Morin-Postel, Sir Robert Smith, Mr F G Steingraber and Mr O H J Stocken all of whom served throughout the period. All the members of the Committee are independent non-executive Directors. During the year, there were six meetings of the Remuneration Committee. Mr F D Rosenkranz and Mme C J M Morin-Postel attended all of these meetings, Sir Robert Smith and Mr F G Steingraber attended five meetings and Mr O H J Stocken attended four meetings.

Details of the work of the Remuneration Committee are set out in the Directors' remuneration report.

Nominations Committee The Nominations Committee comprises Baroness Hogg (Chairman), Mr O H J Stocken, Mr P E Yea, Dr P Mihatsch, Mme C J M Morin-Postel, Mr F D Rosenkranz, Sir Robert Smith and Mr F G Steingraber, all of whom served throughout the period. During the year, there was one meeting of the Nominations Committee which was attended by all members other than Dr P Mihatsch. The terms of reference of the Nominations Committee provide that the Chairman of the Board shall not chair the Committee when dealing with the appointment of the Chairman's successor.

During the year, the Nominations Committee, together with the Board, reviewed the composition of the Board to ensure that the balance of its membership, as between executive and non-executive Directors, and that its profile, in terms of size and length of service and experience of individual Directors, remained appropriate.

A formal, rigorous and transparent process for the appointment of Directors has been established with the objective of identifying the skills and experience profile required of new Directors and identifying suitable candidates. The procedure includes the appraisal and selection of potential candidates, including (in the case of non-executive Directors) whether they have sufficient time to fulfil their roles. Specialist recruitment consultants assist the Committee to identify suitable candidates for appointment. The Committee's recommendations for appointment are put to the full Board for approval.

The Company's major shareholders are offered the opportunity to meet newly-appointed non-executive Directors.

Valuations Committee The Valuations Committee comprises Baroness Hogg (Chairman), Mr O H J Stocken, Mr P E Yea, Mr S P Ball and Dr P Mihatsch, all of whom served throughout the period. Mr M J Queen served as a member of the Committee until 11 May 2005. There were two meetings of the Valuations Committee during the year. The members who served throughout the year attended both meetings, save for Dr P Mihatsch who attended one meeting. Mr M J Queen attended the one meeting held before he ceased to be a Committee member.

During the year, the Valuations Committee considered and made recommendations to the Board on valuations of the Group's investments to be included in the interim and annual financial statements of the Group and reviewed the valuations policy and methodology.

The Company Secretary All Directors have access to the advice and services of the Company Secretary. The Company Secretary is responsible for advising the Board, through the Chairman, on governance matters. The Company's Articles of Association and the schedule of matters reserved to the Board or its duly authorised Committees for decision provide that the appointment and removal of the Company Secretary is a matter for the full Board.

Relations with shareholders The Board recognises the importance of maintaining a purposeful relationship with all its shareholders. The Chief Executive and the Finance Director, together with the Group Communications Director, meet with the Company's principal institutional shareholders to discuss relevant issues as they arise. The Chairman maintains a dialogue with shareholders on strategy, corporate governance and Directors' remuneration as required.

The Board receives reports from the Company's brokers on shareholder issues and non-executive Directors are invited to attend the Company's presentation to analysts and are offered the opportunity to meet shareholders.

The Company also uses its AGM as an opportunity to communicate with its shareholders. At the Meeting, business presentations are made by the Chief Executive and the Finance Director. The Chairmen of the Remuneration, Audit and Compliance, and Nominations Committees are available to answer shareholders' questions.

During the year, at the invitation of the Chairman, the Company's major shareholders met with the Chairman, the Chairmen of the Audit and Compliance Committee and the Remuneration Committee, the Company Secretary and the Finance Director to discuss matters of corporate governance and corporate responsibility relevant to the Company and its shareholders. In addition, a formal survey of the perceptions of the Company's major shareholders was carried out by independent consultants on behalf of the Company. The results of this survey were considered by the Board.

The Notice of the AGM held on 6 July 2005 was dispatched to shareholders not less than 20 working days before the Meeting. At that Meeting, details of proxy votes received (including the number of abstentions) were disclosed in accordance with the Combined Code. These details were subsequently made available on the Company's website. In accordance with the Company's Articles of Association, on a poll every member who is present in person or by proxy has one vote for each share held.

Portfolio management and voting policy In relation to unquoted investments, the Group's approach is to seek to add value to the businesses in which the Group invests through the Group's extensive experience, resources and contacts. In relation to quoted investments, the Group's policy is to exercise voting rights on matters affecting the interests of the Group.

Internal control The Board is responsible for the Group's system of internal control and reviews its effectiveness at least annually. Such a system is designed to manage rather than eliminate the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material misstatement or loss.

Through the regular meetings of the Board and the schedule of matters reserved to the Board or its duly authorised Committees for decision, the Board aims to maintain full and effective control over appropriate strategic, financial, operational and compliance issues. The Board has put in place an organisational structure with clearly defined lines of responsibility and delegation of authority. Each year, the Board considers and approves a strategic plan and an annual budget. In addition, there are established procedures and processes for planning and controlling expenditure and the making of investments. There are also information and reporting systems for monitoring the Group's businesses and their performance.

Risk Committee is a management committee formed by the Chief Executive whose purpose is to review the business of the Group in order to ensure that business risk is considered, assessed and managed as an integral part of the business. There is an ongoing process for identifying, evaluating and managing the Group's significant risks. This process was in place for the year to 31 March 2006 and up to the date of this report. The process is regularly reviewed by the Board and the Audit and Compliance Committee and complies with the internal control guidance for Directors on the Combined Code issued by the Turnbull Committee. The process established for the Group includes:

Policies

- core values, Group standards and Group controls together comprising the Group's high level principles and controls, with which all staff are expected to comply;
- manuals of policies and procedures, applicable to all business units, with procedures for reporting weaknesses and for monitoring corrective action;
- a code of business conduct, with procedures for reporting compliance therewith;

Processes

- appointment of experienced and professional staff, both by recruitment and promotion, of the necessary calibre to fulfil their allotted responsibilities;
- a planning framework which incorporates a Board approved strategic plan, with objectives for each business unit;
- formal business risk reviews performed by management which evaluate the potential financial impact and likelihood of identified risks and possible new risk areas, set control, mitigation and monitoring procedures and review actual occurrences identifying lessons to be learnt;
- a comprehensive system of financial reporting to the Board, based on an annual budget with monthly reports against actual results, analysis of variances, scrutiny of key performance indicators and regular re-forecasting;
- regular treasury reports to the Board, which analyse the funding requirements of each class of assets, track the generation and use of capital and the volume of liquidity, measure the Group's exposure to interest and exchange rate movements and record the level of compliance with the Group's funding objectives;
- a compliance function whose role is to integrate regulatory compliance procedures into the Group's systems;
- well defined procedures governing the appraisal and approval of investments including detailed investment and divestment approval procedures incorporating appropriate levels of authority and regular post investment reviews;

Verification

- an internal audit function which undertakes periodic examination of business units and processes and recommends improvements in controls to management;
- the external auditors who are engaged to express an opinion on the annual financial statements;
- an Audit and Compliance Committee which considers significant control matters and receives reports from the internal and external auditors and the regulatory compliance function on a regular basis.

The internal control system is monitored and supported by an internal audit function which operates on an international basis and reports to management and the Audit and Compliance Committee on the Group's operations. The work of the internal auditors is focused on the areas of greatest risk to the Group determined on the basis of the Group's risk management process. The external auditors independently and objectively review the approach of management to reporting operating results and financial condition. In co-ordination with the internal auditors, they also review and test the system of internal financial control and the information contained in the annual financial statements to the extent necessary for expressing their opinion.

Employment The Group's policy is one of equal opportunity in the selection, training, career development and promotion of employees, regardless of gender, orientation, ethnic origin, religion and whether disabled or otherwise.

The Group treats applicants and employees with disabilities equally and fairly and provides facilities, equipment and training to assist disabled employees to do their jobs. Should an employee become disabled during their employment, efforts are made to retain them in their current employment or to explore the opportunities for their retraining or redeployment within the Group. The Group also provides financial support, through a Company Disability Scheme, to disabled employees who are unable to work.

The Group's principal means of keeping in touch with the views of its employees are through employee appraisals, informal consultations, team briefings, and staff conferences and surveys. Managers throughout the Group have a continuing responsibility to keep their staff fully informed of developments and to communicate financial results and other matters of interest. This is achieved by structured communication including regular meetings of employees.

The Group has clear grievance and disciplinary procedures in place, which include comprehensive procedures on discrimination and the Group's equal opportunities policy. The Group also has an employee assistance programme which provides a confidential, free and independent counselling service and is available to all staff and their families in the UK.

There are clearly defined staff policies for pay and working conditions. The Group's employment policies are designed to provide a competitive reward package which will attract and retain high quality staff, whilst ensuring that the cost element of these rewards remains at an appropriate level.

The Group's remuneration policy is influenced by market conditions and practices in the countries in which it operates. All employees receive a base salary and are eligible for a performance related bonus and to participate in Group share schemes (except in the US) to encourage employees' involvement in the performance of the Group. Investment executives may also participate in investment performance plans, co-investment plans and carried interest schemes, which allow executives to share directly in the future profits on investments. Further details of these plans are set out in the Directors' remuneration report. Employees participate in local state or company pension schemes as appropriate to local market conditions.

Charitable and political donations Charitable donations made by the Group in the year to 31 March 2006 amounted to £390,570. Excluding the Company's matching of Give As You Earn contributions by staff, charitable donations amounted to £290,028, of which approximately 58% were to causes which aim to relieve poverty or benefit the community, or both, approximately 23% were to charities which advance education, and approximately 6% were to medical charities. Further details of charitable donations are set out in the Corporate responsibility section on pages 36 to 41.

In line with Group policy, no donations were made to political parties during the year. Under the Companies Act 1985, as amended, the Company is required to disclose particulars of any donation to any EU political organisation and EU political expenditure incurred during the year. During the period, 3i plc, the main operating company of the Group, made a payment to one organisation, detailed below, which may fall within the definition of donations to EU political organisations. This payment was an annual subscription to the Industry Forum of £3,084.

Policy for paying creditors The Group's policy is to pay creditors in accordance with the CBI Prompt Payers Code of Good Practice, copies of which can be obtained from the Confederation of British Industry at Centre Point, 103 New Oxford Street, London WC1A 1DU. The Company had no trade creditors during the year. 3i plc had trade creditors outstanding at the year end representing on average 15 days purchases.

Statement of Directors' responsibilities The Directors are required by UK company law to prepare financial statements which give a true and fair view of the state of affairs of the Company and the Group as at the end of the period and of the profit for the period. The Directors have responsibility for ensuring that proper accounting records are kept which disclose with reasonable accuracy the financial position of the Group and enable them to ensure that the financial statements comply with the Companies Act 1985. They have a general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities. Suitable accounting policies, which follow generally accepted accounting practice and are explained in the notes to the financial statements, have been applied consistently and applicable accounting standards have been followed. In addition, these financial statements comply with International Financial Reporting Standards as adopted by the European Union and reasonable and prudent judgments and estimates have been used in their preparation.

Going concern The Directors are satisfied that the Company and the Group have adequate resources to continue to operate for the foreseeable future. For this reason, they continue to adopt the "going concern" basis for preparing the financial statements.

Auditors' independence and objectivity Subject to annual appointment by shareholders, auditor performance is monitored on an ongoing basis and formally reviewed every five years, the next review being scheduled for 2008. The Audit and Compliance Committee reviewed auditor performance during the year and concluded that Ernst & Young LLP's appointment as the Company's auditors should be continued.

The Committee recognises the importance of ensuring the independence and objectivity of the Company's auditors. It reviews the nature and extent of the services provided by them, the level of their fees and the element comprising non-audit fees. The Audit and Compliance Committee Chairman is notified of all assignments allocated to Ernst & Young over a set threshold, other than those related to due diligence within the Group's investment process where the team engaged would be independent of the audit team. Safeguards have been put in place to reduce the likelihood of compromising auditor independence, including the following principles which are applied in respect of services provided by the auditors and other accounting firms and monitored by the Audit and Compliance Committee:

- services required to be undertaken by the auditors, which include regulatory returns, formalities relating to borrowings, shareholder and other circulars. This work is normally allocated directly to the auditors;
- services which it is most efficient for the auditors to provide. In this case, information relating to the service is largely derived from the Company's audited financial records; for example, corporate tax services. This work is normally allocated to the auditors subject to consideration of any impact on their independence;
- services that could be provided by a number of firms including general consultancy work. All significant consultancy projects are normally put out to tender and work would be allocated to the auditors only if it did not present a potential threat to the independence of the audit team. Included in this category is due diligence work relating to the investment process. If this service were to be provided by the auditors, the specific team engaged would be independent of the audit team.

Details of the fees paid to the auditors are disclosed in note 6 to the financial statements on page 72.

Audit information Pursuant to section 234ZA (2) of the Companies Act 1985, each of the Directors confirms that: (a) so far as they are aware, there is no relevant audit information of which the Company's auditors are unaware; and (b) they have taken all steps they ought to have taken to make themselves aware of any relevant audit information and to establish that the Company's auditors are aware of such information.

Appointment of auditors In accordance with section 384 of the Companies Act 1985, a resolution proposing the reappointment of Ernst & Young LLP as the Company's auditors will be put to members at the forthcoming Annual General Meeting.

By order of the Board

A W W Brierley

Secretary

10 May 2006

Registered Office

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London SW1E 5JD