

## PRINCIPLES OF GOOD GOVERNANCE

International Power is committed to high standards of corporate governance. In line with the Rules of the UK Listing Authority, the following report explains how the Group has applied the 'Principles of Good Governance' and Code of Best Practice contained in the Combined Code and reports the Group's compliance with the provisions contained in the Code.

### The Board

The Board met on seven occasions during the year. A balance between Executive and Non-Executive Directors underpinned the effectiveness of the Company's Board. In addition to the Non-Executive Chairman, the Board consists of three Executive Directors and three Non-Executive Directors.

All of the Non-Executive Directors are considered to be independent.

In accordance with the Combined Code and the Company's Articles of Association, all Directors submit themselves for re-election at least every three years and newly appointed Directors are subject to election by shareholders at the first opportunity after their appointment. Newly appointed Directors receive comprehensive briefing, and training where appropriate, on the Company and their roles, to ensure that they are fully conversant with their responsibilities.

The Board has responsibility for defining strategy, ensuring the successful implementation of approved plans and for the financial policies of the Group for which it maintains a schedule of all matters requiring specific Board approval. Throughout 2001 this included all strategy decisions and significant capital investment proposals.

The Board receives information on capital expenditure projects and investment proposals in advance of Board meetings, as well as management reports on the operational and financial performance of the business. Financial performance is monitored on a monthly basis and the overall performance of the Group is reviewed against approved budgets.

All of the Directors have access to the advice and services of the Company Secretary and have access to independent advice should they so wish.

The Company has established the following committees: the Audit Committee, the Remuneration and Appointments Committee and the Risk Committee.

*The Audit Committee* (comprising the Chairman and all Non-Executive Directors) is responsible for monitoring the work of the internal audit function and its progress against the Group's annual internal audit plan, and also reviews reports from the external auditors. In addition to reviewing the Group's accounts, results announcements and accounting policies, the Committee monitors the effectiveness of internal control systems for the Board. The Chairman of the Audit Committee is Tony Isaac.

*The Remuneration and Appointments Committee* (comprising the Chairman and all Non-Executive Directors) is responsible, on behalf of the Board, for monitoring the performance of the Executive Directors of the Company and making recommendations to the Board on remuneration, appointments and matters of management succession. The Chairman of the Remuneration and Appointments Committee is Dennis Hendrix.

## Corporate governance

continued

*The Risk Committee* (comprising the Chief Executive Officer, the Chief Financial Officer, the Chief Operating Officer and senior managers) has responsibility, on behalf of the Board, for monitoring the effectiveness of the Group's risk management arrangements. The Committee is also responsible for monitoring health, safety and environmental performance in the Group. The Chairman of the Risk Committee is Philip Cox.

### Relations with shareholders

The Board is accountable to shareholders for the performance and activities of the Group.

International Power ensures that its Annual General Meeting (AGM) provides shareholders with an opportunity to receive comprehensive information on all aspects of the Group's business activities, and to question senior management about business issues and prospects.

All proxy votes are counted and the level of proxy votes lodged for each resolution is reported at the AGM. In line with best practice, the Company aims to ensure that the Notice of the AGM and the *Annual Report* are sent to shareholders at least 20 working days before the AGM.

International Power also runs, within the terms of the regulatory framework, frequent contact programmes with institutional investors, to discuss matters of strategy and financial performance. All results presentations and all Stock Exchange announcements are available to shareholders on the Company's website, [www.ipplc.com](http://www.ipplc.com), in the investor relations section.

### Accountability and audit

The Board is mindful of its responsibility to present a balanced and understandable assessment of International Power's financial position and prospects, in all reports, both to investors and regulatory authorities. The *Annual Report*, interim and quarterly results are the principal means of achieving this objective.

An explanation of the respective responsibilities of the Directors and auditors in connection with the financial statements is set out on page 41. The Directors set out on page 40 the basis for their view that the Group is a going concern.

### Internal control

Systems are in place to meet the requirements of the Combined Code and the Turnbull Guidance for the review of internal controls, including financial, operational and compliance controls and risk management.

The Board has responsibility for the Group's system of internal control and for monitoring its effectiveness. Any system of internal control is designed to manage, rather than eliminate, the risk of failure to achieve business objectives. The system can only provide reasonable, and not absolute, assurance against material financial misstatement or loss. The principal features of the Group's systems of internal control are:

### CONTROL ENVIRONMENT

The Board encourages a culture of integrity and openness. The Company has an organisational structure with clear lines of accountability and authority across its worldwide operations, supported by appropriate reporting procedures. Each of the regional businesses is accountable to the Chief Executive through the Chief Operating Officer and is managed within the strategic guidelines and delegated authorities adopted by the Board.



Pelican Point,  
South Australia

Bellingham,  
Massachusetts, US

## CONTROL PROCEDURES

Control procedures have been established in each of the Company's operations to safeguard the Group's assets from loss or misuse and to ensure appropriate authorisation and recording of financial transactions. Risk management procedures are in place for the Company's operations, including its energy marketing and trading activities, which are overseen by the Global Risk Manager. The Group treasury function operates under defined policies and the Treasury Committee, chaired by the Chief Financial Officer, monitors its activities. All acquisition and development decisions are subject to disciplined investment appraisal processes.

## PERFORMANCE REPORTING AND INFORMATION

*Corporate plan* Executive management submits an annual corporate plan to the Board for approval. The plan for each business unit is the quantified assessment of its planned operating and financial performance for the next financial year, together with strategic reviews of the following four years. Group Management review the plans with each operational team. The individual plans are based on key economic and financial assumptions and incorporate an assessment of the risks and sensitivities underlying the projections.

*Performance monitoring* Monthly performance and financial reports are produced for each business unit, with comparisons to budget. Reports are consolidated for overall review by executive management, together with forecasts for the profit and loss account and cash flow. Detailed reports are presented to the Board on a regular basis.

*Performance review* Each business unit is subject to a performance review with Group Management regularly during the year. Actual results are compared to budget and to financial forecasts. Key operational and financial metrics are reviewed together with the risk profile and business environment of the reporting unit.

*Investment projects* These are subject to formal review and authorisation procedures with designated levels of authority. Major projects are subject to Board review and approval.

## RISK IDENTIFICATION AND MANAGEMENT

There is a continuous process for identifying, evaluating and managing the key risks faced by the Company. Activities are co-ordinated by the Risk Committee, which has responsibility for ensuring the adequacy of systems for identifying and assessing significant risks, that appropriate control systems and other mitigating actions are in place, and that residual exposures are consistent with the Company's strategy and objectives. Assessments are conducted for all material entities.

As part of the annual business planning process, the key risks associated with achievement of principal objectives are identified and their impact quantified. During the year, significant changes in the risk profile are highlighted through the business performance reports. The principal risks are reviewed by the Risk Committee, which provides regular reports to the Board.

For each of the businesses that operate in traded energy markets, local risk committees have been established to oversee the management of the market, operational and credit risks arising from the marketing and trading activities. These committees are chaired by the Global Risk Manager and comprise Executive Directors and senior managers.

### ENERGY MARKETING AND TRADING

The principal objective of the Group's energy marketing and trading operations is to maximise the return from selling the physical output of its plants.

The Group hedges its physical generating capacity by selling forward its output, and purchasing its input, as and when commercially appropriate and within approved control limits. This is accomplished through a range of physical off-take and supply arrangements. Our limited proprietary trading operations use a range of financial and physical products.

Energy market risk on our asset and proprietary portfolios is measured using value at risk and other methodologies. Value at risk provides a fair estimate of the net losses or gains which could be recognised on our portfolios over a certain period and given a certain probability; it does not provide an indication of actual results. It is routinely checked for accuracy against actual movements in the portfolio value.

In addition to using value at risk measures, we perform scenario analyses to estimate the economic impact of sudden market movements on the value of our portfolios. This supplements the value at risk methodology and captures additional market risks.

### MONITORING

The Board reviews the effectiveness of established internal controls through the Audit Committee, which receives reports from management, the Risk Committee, the Group's internal audit function and the external auditors on the systems of internal control and risk management arrangements.

Internal audit reviews the effectiveness of internal controls and risk management through a work programme based on the Company's objectives and risk profile. Findings are reported to operational and executive management, with periodic reporting to the Audit Committee.

Annual self-certification statements of compliance with procedures are provided by business unit managers. These statements give assurance that controls are in operation and confirm that programmes are in place to address any weaknesses in internal control. The certification process embraces all areas of material risk. The internal audit function reviews the statements and reports any significant issues to the Audit Committee.

### Compliance with the Combined Code

At this stage of the Company's development, the Board believes that the Chief Executive Officer's fixed three-year service contract is appropriate, given his experience and knowledge of the market in which the Group operates. His remuneration is paid entirely in shares as described in the Remuneration report. The service contracts for the other Executive Directors reverted to a 12-month notice on 2 October 2001.

In all other respects, the Company has complied with the provisions of the Combined Code throughout the period of the review.

We have considered the ABI guidelines on corporate social responsibility, which were issued in October 2001. It is our intention to seek to comply with them in our 2002 *Annual Report*.