

## Corporate Governance

The Board is committed to maintaining the highest standards of corporate governance. This commentary describes how the Group applies the main and supporting principles of section 1 of the 2006 Combined Code on Corporate Governance, which sets out principles of good governance and a code of best practice.

Our policy on corporate governance is as follows:

### Board role and responsibilities

Your Board has overall responsibility for the leadership and control of the Group. Responsibility for the management of the Group has been delegated by the Board to executive management. This delegation is effected through the Chief Executive, who is accountable to the Board for its exercise. The functions of Chairman and Chief Executive are not combined and both roles' responsibilities are clearly divided. A number of responsibilities of the Board are delegated to committees of the Board.

Certain decisions of the Group are formally reserved to the Board. The Board has responsibility for approving Group strategy, annual budgets, major acquisitions and capital projects, and treasury policy. It sets governance policies and ensures implementation thereof. It defines the roles and responsibilities of the Chairman, Chief Executive, other directors and the Board sub-committees. It appoints and removes directors from the boards of the Company and its subsidiary companies. In addition, the Board approves the interim and annual financial statements, reviews the Group's systems of internal control and approves any significant changes in accounting policies. It approves all resolutions and related documentation put before shareholders at general meetings. The Board sets the Group's dividend policy, approves the interim dividend and recommends the final dividend.

In addition to the matters formally reserved to the Board, regular contact by the directors with each other, and availability to the Chairman and to the Chief Executive for advice and ideas, remain critical. Effective Paddy Power Board members are enthusiasts for the business. Mere attendance at meetings is not sufficient, what matters is the director's active participation and contribution in these meetings.

The non-executive directors also meet once a year without their executive director colleagues or your Chairman.

Individual directors may seek independent professional advice, at the expense of the Company, in the furtherance of their duties as a director. The Company has also arranged appropriate insurance cover in respect of legal action against the directors.

### Board composition

The Board should comprise a mix of the necessary business skills required to provide oversight of the management of the business and to contribute to the development and advancement of business strategy. Paddy Power is a specialist business and should always retain the betting industry savvy that has been part of the fabric of its Board, both as a private and public company. The Board should also include high quality non-executives sourced from the different geographic markets in which the Group operates. The majority of the Board should be independent non-executive directors.

It is essential that all Board members have sufficient time to add real value to your Company. With this in mind and, reflecting the regulatory obligations and the wider demands of this Board, it has been agreed that, unless otherwise agreed by the Board, our non-executive directors should not hold more than three directorships of publicly quoted companies. In addition, the Chairman cannot be the chairman of any other publicly quoted company. We have also agreed that there should be no more than two Paddy Power directors on the Board of any one other listed company. Unless otherwise agreed by the Board, executive directors should hold non-executive directorships with no more than one other publicly quoted company.

### Tenure

The current Board comprises a mix of executive directors, founding directors and directors recruited for the particular skill and experience they would bring to Paddy Power. Of the ten directors currently serving on the Board, just two have been members since the Company was launched on the Stock Exchange in December 2000. The Board expects to appoint one additional independent non-executive director in 2009 and another in 2010.

The standard terms of the letter of appointment of non-executive directors is available, on request, from the Company Secretary.

### Directors' independence

As stated in the Directors' Report on page 26, Mr Pádraig Ó Ríordáin was appointed as a non-executive director in July 2008. In considering his appointment, the Board evaluated Pádraig's independence, given his role as Managing Partner of Arthur Cox, which is one of the Group's legal advisors. The Board concluded that notwithstanding this relationship, Pádraig is independent in character and judgment. He has a demonstrated record of such independence, including his appointment by the Minister for Finance to the Irish Government's Advisory Forum on Financial Legislation, on which he serves as Independent Chairman, and the role of Managing Partner which he plays at his firm. The Board took account of the fees paid to Arthur Cox for its legal services and concluded that they are not material to Pádraig's independent judgment given the scale of the operations and financial results of Arthur Cox and the Group. Pádraig has not provided any legal services to the Group since his appointment to the Board.

The Board concluded that Pádraig is an independent non-executive director within the spirit and meaning of the Combined Code on Corporate Governance.

### The Chairman's role

The Chairman is responsible for the leadership of the Board, ensuring its continued effectiveness in carrying out its duties and setting its agenda. The Chairman is also responsible for ensuring that all directors receive accurate, timely and clear information. The Chairman facilitates the effective contribution of his non-executive colleagues and ensures constructive relationships exist between executive and non-executive directors. He is the guarantor of effective communications with shareholders.

While there may be a perception that Board business revolves exclusively around meetings, this is not the case. Board counsel must be available to senior management at all times. Your Chairman is the normal source of such advice and encouragement, but by no means the only one. The need to source the most relevant expertise at short notice means that the Chairman must have regular contact with individual Board members to ensure that there is a seamless interaction between the senior executive team and the non-executive directors.

As Chairman, I also meet with the non-executive directors independently of the executive directors. I meet regularly with the Chief Executive to discuss all aspects of the business's performance and, on an occasional basis, we meet with other senior members of the management team together.

#### Directors' fees

As reported in the 2007 Annual Report, the standard non-executive fee was set at €70,000 in 2008. It was also agreed that the Audit Committee chair would receive an additional fee of €20,000, that chairs of other Committees would be paid an additional fee of €12,000 and that the Chairman would receive an annual fee of €200,000.

These fees were set for a two year period and, barring exceptional circumstances, will not be reviewed again until 2010.

Non-executive directors are not eligible to participate in the Group bonus schemes, option plans or share award schemes. None of the remuneration of the non-executive directors is performance related. The non-executive directors' fees are not pensionable and non-executive directors are not eligible to join any Group pension plans.

#### Board effectiveness

Each director is expected to perform to the highest standards with regard to both their general contribution and their contribution through committees and mentoring.

As Chairman, it is my responsibility to ensure that the performance of all directors is at the levels required. A performance evaluation of the Board, its committees and its individual directors is undertaken annually. I will act on the results of the performance evaluation by recognising the strengths and addressing the weaknesses of the Board and, where appropriate, appointing new members to the Board or seeking the resignation of existing directors. The Senior Independent Director will conduct a detailed review of my performance as Chairman at the end of my first year in the role.

#### Board operations and committees

The Board holds at least eight full Board meetings each year and each non-executive member of the Board sits on at least one committee. I expect all Board members to be available to me between meetings.

The composition of the Board committees as at 27 February 2009 was as follows:

#### Audit

Tom Grace (Chair); Pádraig Ó Ríordáin; Brody Sweeney.

#### Remuneration

Pádraig Ó Ríordáin (Chair); Nigel Northridge.

#### Nomination

Nigel Northridge (Chair); Fintan Drury; Patrick Kennedy; Stewart Kenny; Brody Sweeney.

#### Risk

David Power (Chair); Breon Corcoran; Patrick Kennedy; Stewart Kenny.

#### Audit Committee

The Audit Committee's responsibilities include:

- monitoring the integrity of the financial statements of the Company and Group;
- reviewing the Group's internal controls;
- monitoring and reviewing the effectiveness of the Group's internal audit function;
- making recommendations to the Board in relation to the appointment and removal of the Group's external auditor;
- approving the remuneration and terms of engagement of the external auditor;
- evaluating the performance of the external auditor, including their independence and objectivity;
- approving non-audit services provided by the auditor in accordance with the Group's policy on non-audit services;
- developing and ensuring compliance with the Group's policy on the provision of non-audit services;
- reviewing arrangements by which staff may, in confidence, raise concerns about possible improprieties in matters of financial reporting or other matters; and
- ensuring that there are appropriate procedures in place to monitor and evaluate the general business risks to which the Group is exposed.

The Audit Committee has unrestricted access to the Group's external and internal auditors, with whom it meets at least twice a year, both with and without management. These meetings ensure that there are no restrictions on the scope of their audits, and allow discussion of any matters that the auditors did not wish to raise in the presence of management.

The Audit Committee is responsible for ensuring that external auditor objectivity and independence is safeguarded where the auditor also provides non-audit services to the Group. The Audit Committee reviewed the letter from the Group's external auditor confirming their independence and objectivity. During the year, the Committee also performed a review of the audit and non-audit services provided by the external auditor, and the fees charged for those services, to ensure there was no impairment of independence.

# Corporate Governance

(continued)

## Remuneration Committee

The Remuneration Committee is primarily responsible for making recommendations to the Board on remuneration policy for the Group's executive directors and selected senior management. The report of the Remuneration Committee is set out on pages 33 and 34.

## Nomination Committee

The Nomination Committee is primarily responsible for recommending candidates to the Board for appointment as directors and ensuring that appropriate procedures are followed for all such appointments.

In appointing new non-executive directors, although it has made some use of external search consultancies, the primary method used by the Committee has been to agree the preferred profile of the director with the Board as a whole and receive written recommendations from existing directors. Given the industry knowledge of the Board and the Committee members, as well as their general commercial experience, this has proved an effective method of sourcing high quality directors for your Company.

## Risk Committee

The Risk Committee is responsible for ensuring that policies in respect of betting risk are appropriate to a group of Paddy Power's size, for monitoring that such policies are being correctly applied and that the expertise and systems within the organisation are consistent with the level of risk undertaken. The Committee also sets overall policy for betting risk. Limits are agreed with the Committee and set annually but are subject to review by the Committee at any time. Compliance with these risk limits is reported daily to senior management and internal audit. Internal audit also carries out reviews of the risk function. The Group does not offer credit betting.

## Attendance at Board and Committee meetings

There were eight full meetings of the Board in 2008.

The attendance at Board and committee meetings by the directors who held office in 2008 are set out below:

	Note	Board	Audit	Remuneration	Nomination	Risk
Number of meetings held in 2008:		8	5	7	4	2
Attended by:						
F Drury *		8		7	3	
N Northridge *		8		7	4	
T Grace *		8	5			
B Sweeney *		7	4			
D Power **	a)	8	3	4		2
S Kenny **		8			4	2
P Ó Riordáin *	b)	3	2	3		
P Kennedy ***		8			4	2
J Massey ***		8				
B Corcoran ***		8				2

\* Independent non-executive director

\*\* Non-executive director

\*\*\* Executive director

a) David Power was a member of the Audit Committee and chair of the Remuneration Committee until 21 August 2008. There were three Audit Committee and four Remuneration Committee meetings prior to that date, all of which he attended.

b) Pádraig Ó Riordáin was appointed as a director on 8 July 2008 and as a member of the Audit Committee and chair of the Remuneration Committee on 21 August 2008. There were three Board meetings, two Audit Committee meetings and three Remuneration Committee meetings after his appointments, all of which he attended.

The number of independent non-executive directors is now five (including the Chairman) and there are five non-independent directors (including three executive directors). The Combined Code requires a majority of the Board to be independent non-executive directors.

Until the appointment of Pádraig Ó Ríordáin as a member of the Audit Committee on 21 August 2008, the Audit Committee was not populated in accordance with the Combined Code as the Committee did not consist of a majority of independent directors. Since his appointment, the Audit Committee has been populated in accordance with the Combined Code.

At 31 December 2008 and throughout the year, the Nomination Committee was not populated in accordance with the Combined Code as it did not consist of a majority of independent non-executive directors. Brody Sweeney was appointed as a member of the Nomination Committee on 24 February 2009 and since his appointment, the Committee has been populated in accordance with the Combined Code.

The Board is in a state of transition and it is currently not possible to populate the Remuneration Committee in accordance with the Combined Code. The Group is committed to complying with corporate best practice and expects to complete the appointment of one additional non-executive director in 2009 and another in 2010.

#### Senior Independent Director

The Board appointed Tom Grace as Senior Independent Director in January 2009, on Nigel Northridge becoming Chairman. Tom is available to shareholders who have concerns that cannot be addressed through the Chairman, Chief Executive or Finance Director.

#### Company Secretary

The appointment and removal of the Company Secretary is a matter for the Board. All directors have access to the advice and services of the Company Secretary, who is responsible to the Board for ensuring that Board procedures are complied with.

#### Internal control

The Combined Code on Corporate Governance states that:

1. The Board should maintain a sound system of internal control to safeguard shareholders' investment and Group assets.
2. The directors should, at least annually, conduct a review of the effectiveness of the Group's system of internal control and should report to shareholders that they have done so. The review should cover all material controls, including financial, operational and compliance controls, and risk management systems.

The directors have overall responsibility for the Group's system of internal control and have delegated responsibility for the implementation of this system to executive management. This system includes financial controls which enable the Board to meet its responsibilities for the integrity and accuracy of the Group's accounting records.

The Board has also established a process of compliance which addresses the Board's responsibility to maintain, review and report on all internal controls.

The principal processes comprising the system of internal control are:

- budgets are prepared for approval by executive management and include a Group budget approved by the Board;
- income and expenditure are regularly compared to previously approved budgets;
- the Board establishes appropriate treasury risk policies for implementation by executive management. Compliance with risk limits is reported on by the risk management department and reviewed by senior management and internal audit;
- all material commitments for expenditure and payments are compared to previously approved budgets and are subject to prior approval by personnel designated by the Board of Directors;
- regular financial results are submitted to and reviewed by the Board of Directors;
- the directors, through the Audit Committee, review the effectiveness of the Group's system of internal control; and
- an audit and security department, independent of operations, monitors the activities of the betting operations and the risk management division, including the verification of winning bets. They also undertake internal control reviews throughout the Group. The head of this department meets regularly with the Audit Committee.

The Board, through the Audit Committee, is responsible for conducting a review of the effectiveness of the Group's systems of internal controls. This review has been performed in respect of the year ended 31 December 2008. The directors consider that the procedures necessary to implement the Turnbull guidelines on internal control in the Combined Code have been properly established.

# Corporate Governance

(continued)

## Relations with shareholders

The Group is committed to ongoing communication with its shareholders. The Group operates an investor relations section on its corporate website ('www.paddypowerplc.com'). This contains copies of investor presentations and annual reports as well as providing access to Regulatory News Service ('RNS') statements and corporate press releases. All shareholders are encouraged to attend the Annual General Meeting where they are afforded the opportunity to question the Board.

There is regular discussion between Group management and analysts, brokers and institutional shareholders, ensuring that the market is appropriately informed on business activities. Visits to the Group's headquarters are encouraged and tours of our retail outlets are undertaken regularly. Feedback from major shareholders and reports by analysts are communicated to directors so directors can monitor their views on the Group.

The short-term financial performance of Paddy Power can be significantly influenced throughout the financial year by the run of sporting results. This is normal in the sports betting industry. For example, a disproportionate number of favourites winning at a major horse racing festival will depress short-term profitability, whereas a disproportionate number of outsiders winning will have the opposite effect. The experience of the industry is that this typically balances out over a more extended period. Accordingly, the Board does not believe that the typical levels of short-term profit volatility intrinsic to our business should significantly influence the investment decisions of a reasonable investor or that it should be likely to have a significant effect on the Company's share price.

The Board and management of Paddy Power carefully monitor any significant variances in financial performance to assess, based on the experience of the Company, whether such variances are attributable to the run of sporting results and therefore likely to be short-term in nature or reflect a trend which may impact on the overall performance of the Company going forward. The Board considers these two categories of variances to be fundamentally different as to their likely influence on the investment decisions of a reasonable investor and therefore on the Company's share price. The Board makes its judgments in respect of announcements to the market and its obligations under the disclosure rules to which the Company is subject against this background.

## Compliance

The directors confirm that the Company has complied throughout the accounting period with the provisions of the Combined Code, except as noted in this commentary.

## Conclusion

I would invite you all to consider the above carefully, and encourage any shareholders who have questions relating to this Corporate Governance statement to contact me by email at [nnorthridge@paddypower.com](mailto:nnorthridge@paddypower.com).



**Nigel Northridge**

*Chairman*

27 February 2009