

CORPORATE GOVERNANCE REPORT

Johnson Electric is committed to achieving high standards of corporate governance that properly protect and promote the interests of its shareholders and devotes considerable effort to identifying and formalising best practices of corporate governance.

BOARD OF DIRECTORS

As at 31st March 2006, Johnson Electric's Board consisted of three executive directors and eight non-executive directors (of whom six are independent).

The independent non-executive directors, who represent a majority of the Board, are all experienced individuals from a range of industries and geographies. Their mix of professional skills and experience is an important element in the proper functioning of the Board and in ensuring a high standard of objective debate and overall input to the decision-making process. The Board has received from each independent non-executive director a written confirmation of their independence and has satisfied itself of such independence up to the approval date of this report in accordance with the Rules Governing the Listing of Securities (the "Listing Rules") on The Stock Exchange of Hong Kong Limited (the "Stock Exchange").

The biographical details of the directors are provided on pages 43 to 48 of this report.

THE BOARD AT WORK

The Board of directors is accountable to shareholders for the activities and performance of the Group. It meets in person on a quarterly basis and on other occasions when a board-level decision on a particular matter is required. The Board has reserved for its decision or consideration matters covering corporate strategy, annual and interim results, directors' appointment, succession planning, risk management, major acquisitions, disposals and capital transactions, and other significant operational and financial matters.

The majority of board meetings are scheduled to last one full day, with directors receiving details of agenda items for decision and minutes of committee meetings in advance of each board meeting.

Although the capacity of any board to involve itself in the details of a large international business is limited, Johnson Electric aims to provide its independent non-executive directors with extensive exposure and access to its operations and management. Over the past four years, the number and duration of board meetings have increased and the board agenda is structured to address the broad spectrum of key governance issues on a regular and systematic basis. Forming part of the continuous professional development programme for directors, visits to the Company's principal operating facilities have been arranged and professional guest speakers are invited to address the Board from time to time.

Major corporate matters that are specifically delegated by the Board to management include the preparation of annual and interim accounts for board approval before public reporting, execution of business strategies and initiatives adopted by the Board, implementation of adequate systems of internal controls and risk management procedures, and compliance with relevant statutory requirements and rules and regulations.

The Group's General Counsel and Chief Financial Officer also attend all board meetings to advise on corporate governance, risk management, statutory compliance, mergers and acquisitions, and accounting and financial matters.

Under the Company's Bye-Law 109(A), one-third of the directors except the executive chairman, who have served longest on the Board, must retire, thus becoming eligible for re-election at each Annual General Meeting. As such, except the executive chairman, no director has a term of appointment longer than three years.

The Company has arranged for appropriate liability insurance to indemnify its directors for their liabilities arising out of corporate activities. The insurance coverage is reviewed on an annual basis.

COMMITTEES

The monitoring and assessment of certain governance matters are allocated to four committees which operate under defined terms of reference and are required to report to the full Board on a regular basis. The composition of the committees during 2005/06 and up to the date of this report is set out in the table below.

Directors	Audit Committee	Remuneration Committee	Nomination And Corporate Governance Committee	Board Committee
Executive Directors				
Patrick Shui-Chung Wang			M	M
Winnie Wing-Yee Wang		M		M
Independent Non-Executive Directors				
Peter Stuart Allenby Edwards			C	
Patrick Blackwell Paul	C		M	
Arkadi Kuhlmann		C		
Laura May-Lung Cha	M			
Oscar De Paula Bernardes Neto		M		
Michael John Enright	M			

C – Chairman

M – Member

AUDIT COMMITTEE

The Audit Committee is comprised of three independent non-executive directors who together have substantial experience in the fields of accounting, business, corporate governance and regulatory affairs.

The committee is responsible for monitoring the reporting, accounting, financial and control aspects of the executive management's activities. It has full access to the Group's Internal Audit Director to hear directly any concerns of the internal audit department that may have arisen during the course of the department's work. The committee also monitors the appointment and function of the Group's external auditor. The committee's authority and duties are set out in written terms of reference and are posted on the Company's website.

Three Audit Committee Meetings were held in 2005/06 to discuss and review the following matters together with the Chief Financial Officer, Internal Audit Director and the external auditors:

1. the review of the FY2005 annual results and interim results for FY2006, and to consider that the related disclosures in the financial statements were complete, accurate and fair, and complied with accounting standards, stock exchange and legal requirements, and to submit the same to the board for approval;
2. consideration of the principal accounting policies adopted by the Group;
3. consideration of the work done by the internal and external auditors, the relevant fees and terms, results of audits performed by the external auditors and appropriate actions required on significant control weaknesses;
4. the review of the external auditors' independence and recommendation to the board the re-appointment of the external auditors at the 2005 annual general meeting;
5. the review of the Group's report on compliance with laws and regulations in the countries in which it operates;
6. the review of the Internal Audit Department's audit plan and ongoing progress reports;
7. the review of the adequacy and effectiveness of the internal control and risk management systems;
8. consideration of the provision of non-audit services by the external auditors; and
9. the review of the revised terms of reference of the Audit Committee for conformity with the Listing Rules.

REMUNERATION COMMITTEE

The Remuneration Committee is comprised of two independent non-executive directors (including the Committee Chairman) and one executive director.

The committee determines the compensation structure and rewards for the Chief Executive and other executive directors and monitors the policies being applied in remunerating other senior executives in the Group. In addition, it has responsibility for reviewing and making appropriate recommendations to the Board on management development and succession plans for executive directors and senior management levels. The committee's authority and duties are set out in written terms of reference and are available on the Company's website.

The fundamental policy underlying Johnson Electric's remuneration and incentive schemes is to link total compensation for senior management with the achievement of annual and long-term performance goals. By providing total compensation at competitive industry levels for delivering on-target performance, the Company seeks to attract, motivate and retain key executives essential to its long-term success. Senior management incentive schemes include an equity component that is designed to align the long-term interest of management with those of shareholders.

Two committee meetings were held in 2005/06. During the financial year, the committee addressed the following:

1. Annual Incentive Plan (AIP) for senior management: reviewed performance and approved the payment for 2004/05 financial year; also approved the plan revisions for 2005/06 and onwards which will better align the AIP to international market competitiveness;
2. Long term incentive plan for senior management: approved the inclusion of non-expatriate senior management in the stock award plan, which was originally designed and approved for expatriate senior management;
3. Remuneration levels for executive directors: reviewed the philosophy for remunerating executive directors;
4. Remuneration packages and service contracts for senior management: reviewed and approved; and
5. Senior management movement and sourcing of senior management: reviewed and discussed.

One of the key mandates of the committee is to establish a market competitive total remuneration program for senior management and key employees for purposes of attracting, motivating and retaining top international leadership talent. To that end, the committee also stays abreast of current and emerging market trends in North America and Europe, regions from which the Group sources many of its senior management talent. The composition of the committee membership reflects this commitment to an international perspective.

All staff positions, including senior management, are sized based on a job evaluation methodology which takes into account management / technical know-how, problem solving and accountability. Individual senior management remuneration acknowledges individual responsibility, contribution and performance. The base salary takes into account factors such as job value, retention and, for those who have recently been hired, previous remuneration. The annual incentive plan, when payable, is in addition to the basic salary and is entirely performance-based and has both financial and non-financial objectives. The long term incentive plan is an annual award of Johnson Electric stock given to senior management and subject to vesting based upon Group service. It is used both as a retention and as a motivation tool and is designed to maximize long-term shareholder value.

In determining the level of remuneration and fees paid to members of the Board of Directors, a survey of current practices in leading Hong Kong listed companies was conducted. The structure essentially consists of a base remuneration with additional fees payable for attendance at certain committee meetings. Executive directors are not eligible for additional remuneration or fees for Board activities.

No individual director or senior management is involved in approving his or her own remuneration.

In addition to international market competitiveness, the effectiveness of the overall remuneration program could be enhanced if there were programs in place to meet both the basic (hygiene factor) and the motivational (reward) requirements in terms of a short, medium and long term time horizon. The committee ensures that the overall program is comprehensive, balanced and responsive to individual needs.

NOMINATION AND CORPORATE GOVERNANCE COMMITTEE

The Nomination And Corporate Governance Committee is comprised of two independent non-executive directors (including the Committee Chairman) and one executive director.

The committee is responsible for the identification and evaluation of candidates for appointment or reappointment as a director, as well as the development and maintenance of the Group's overall corporate governance policies and practices. The committee's authority and duties are set out in written terms of reference and are posted on the Company's website.

The Company follows a formal, fair and transparent procedure for the new appointment of directors to the Board. The committee will first consider necessary changes in respect of the structure, size and composition of the Board, identify suitably qualified candidates by considering their professional knowledge and industry experience, personal ethics, integrity and personal skills and time commitments, and makes recommendation to the Board for decision. In accordance with the Bye-Laws of the Company, every newly appointed director is subject to re-election at the following annual general meeting.

No new directors were nominated in 2005/06.

During the financial year, the committee met on two occasions. The following is a summary of work performed by the committee during the financial year:

1. Consideration and recommendation of the retiring directors for re-election at the annual general meeting;
2. the review and approval of the revised terms of reference of the committee;
3. the review of the structure and composition of the Board;
4. consideration of the independence of all the independent non-executive directors; and
5. a detailed review of the new corporate governance provisions in the Listing Rules.

BOARD COMMITTEE

The Board Committee is comprised of two executive directors. Its primary function is to undertake and supervise the day to day management and operating affairs of the Group. It exercises leadership and develops and keeps under review strategy and business development initiatives of the Group and supervises their implementation.

BOARD AND COMMITTEE ATTENDANCE

The Board held five full board meetings in 2005/06 and the average attendance rate was 89%. Details of the attendance of individual directors at board meetings and committee meetings during the 2005/06 financial year are set out in the table below:

Directors	No. of meetings attended / held			
	Full Board Meeting	Audit Committee	Remuneration Committee	Nomination And Corporate Governance Committee
Executive Directors				
Patrick Shui-Chung Wang <i>(Chairman and Chief Executive)</i>	5/5	–	–	2/2
Winnie Wing-Yee Wang <i>(Vice-Chairman)</i>	5/5	–	2/2	–
Richard Li-Chung Wang <i>(Executive Director)</i>	5/5	–	–	–
Non-Executive Directors				
Yik-Chun Koo Wang <i>(Honorary Chairman)</i>	2/5	–	–	–
Peter Kin-Chung Wang	3/5	–	–	–
Independent Non-Executive Directors				
Peter Stuart Allenby Edwards	5/5	–	–	2/2
Patrick Blackwell Paul	5/5	3/3	–	2/2
Arkadi Kuhlmann	5/5	–	2/2	–
Laura May-Lung Cha	5/5	3/3	–	–
Oscar De Paula Bernardes Neto	4/5	–	2/2	–
Michael John Enright	5/5	3/3	–	–
Average attendance rate	89%	100%	100%	100%
Dates of meetings	13/06/2005 24/08/2005 09/09/2005 05/12/2005 24/03/2006	07/06/2005 18/10/2005 28/11/2005	13/06/2005 27/07/2005	13/06/2005 05/12/2005

INTERNAL CONTROL AND RISK MANAGEMENT

The Board is responsible for ensuring that a sound and effective system of internal controls is maintained within the Group, and for reviewing its effectiveness through the Audit Committee.

The internal control system, which includes a defined management structure with specified limits of authority, is designed to (a) help the achievement of business objectives, and safeguard the Group's assets; (b) ensure proper maintenance of accounting records and reliability of financial reporting; and (c) ensure compliance with relevant legislation and regulations.

The internal control system is designed to provide reasonable, but not absolute, assurance against material misstatement or loss and to manage, but not to eliminate, risks of failure in achieving the Group's objectives.

In accordance with the code provisions on internal control under Appendix 14 of the Listing Rules published by the Stock Exchange, the Board confirms that ongoing processes to identify and manage key risks to the achievement of the Group's strategic objectives are an integral part of the internal control environment. Such processes include strategic planning, the appointment of senior management, the regular monitoring of performance, control over capital expenditure and investments and the setting of high standards and targets for safety, health and environmental performance.

The management maintains and monitors the system of controls, including financial, operational, compliance controls and risk management functions, on an ongoing basis.

The Group's internal audit department, under the supervision of the Director, Internal Audit, independently reviews these controls and evaluates their adequacy, effectiveness and compliance. Audit findings and recommendations are reported to the Audit Committee, Executive Committee members, and the external auditors. In addition, progress on audit recommendations implementation is followed up on a monthly basis. The results are discussed with the Audit Committee on a periodic basis.

Based on the results of evaluations and representations made by the management, the Group's internal audit department and external auditors in 2005/06, the Audit Committee is satisfied that:

- there is an ongoing process for identifying, evaluating and managing the significant risks faced by the Company that threaten the achievement of its business objectives;
- a proper system of internal control has been in place in FY2006, and up to the date of approval of the annual report; and
- the system of internal control has been subject to adequate review during the year.

EXTERNAL AUDITOR

Johnson Electric's independent external auditor is PricewaterhouseCoopers. The Audit Committee is responsible for considering the appointment of the external auditor and also reviews any non-audit functions performed by the external auditor for the Group. In particular, the committee will consider, in advance of them being contracted for and performed, whether such non-audit functions could lead to any potential material conflict of interest.

During the 2005/06 financial year, the services (and associated remuneration) provided by PricewaterhouseCoopers to the Group were as follows:

	2005/06	2004/05
	US\$M	US\$M
Audit	1.88	0.77
Taxation	0.31	0.31
Other services	1.49	0.26

COMMUNICATIONS WITH SHAREHOLDERS

Johnson Electric uses a number of formal communications channels to account to shareholders for the performance of the Company. These include the Annual Report and Accounts, the Interim Report, periodic company announcements made through the Stock Exchange, as well as through the Annual General Meeting. Copies of relevant corporate and financial information are also made available through the Company's website: *www.johnsonelectric.com*.

The Company aims to provide its shareholders and potential investors with high standards of disclosure and financial transparency. In order to provide effective disclosure to investors and potential investors and to ensure they all receive equal access to the same information at the same time, information considered to be of a price sensitive nature is released by way of formal public announcements as required by the Listing Rules. The Company supplements and follows up such announcements through periodic presentations, investor road shows, and conference calls with the international investment community. The Company also welcomes comments and questions from shareholders at its Annual General Meeting.

CODE ON CORPORATE GOVERNANCE PRACTICES

During the year ended 31st March 2006, the Company had complied with the code provisions set out in the Code on Corporate Governance Practices contained in Appendix 14 of the Listing Rules, except for the following deviations:

Code Provision A.2.1

Code A.2.1 provides, inter alia, that the roles of chairman and chief executive officer should be separate and should not be performed by the same individual.

Neither the Company's Bye-Laws nor The Johnson Electric Holdings Limited Company Act, 1988 (a private act of Bermuda) contains any requirement as to the separation of these roles.

Dr. Patrick Shui-Chung Wang is the Chairman and Chief Executive of the Company. The Board is of the opinion that it is appropriate and in the best interests of the Company at its present stage of development that Dr. Wang should hold both these offices. The Board, which is comprised of a majority of independent non-executive directors, believes that it is able effectively to monitor and assess management in a manner that properly protects and promotes the interests of shareholders.

Code Provision A.4.1 and A.4.2

Code A.4.1 provides, inter alia, that non-executive directors should be appointed for a specific term, subject to re-election.

Code A.4.2 also provides that every director, including those appointed for a specific term, should be subject to retirement by rotation at least once every three years.

The independent non-executive directors were appointed for a specific term while the non-executive directors do not have a specific term of appointment. However, under Section 3(e) of The Johnson Electric Holdings Limited Company Act, 1988 and the Company's Bye-Law 109(A), one-third of the directors who have served longest on the Board must retire thus becoming eligible for re-election at each Annual General Meeting. Accordingly, no director has a term of appointment longer than three years. Bye-Law 109(A) states that the executive chairman is not subject to retirement by rotation and shall not be counted in determining the number of directors to retire.

In the opinion of the Board, it is important for the stability and beneficial to the growth of the Company that there is, and is seen to be, continuity of leadership in the role of the Chairman of the Company and, in consequence, the Board is of the view that the Chairman should not be subject to retirement by rotation or hold office for a limited term at the present time.

MODEL CODE FOR SECURITIES TRANSACTIONS

The Group has adopted procedures governing directors' securities transactions in compliance with the Model Code as set out in Appendix 10 of the Listing Rules. Specific confirmation has been obtained from all directors to confirm compliance with the Model Code throughout the year ended 31st March 2006. No incident of non-compliance was noted by the Company to date in 2005/06.

Employees who are likely to be in possession of unpublished price-sensitive information of the Group are also subject to compliance with guidelines on no less exacting terms than the Model Code.

DIRECTORS' AND AUDITORS' RESPONSIBILITIES FOR ACCOUNTS

The Directors' responsibilities for the accounts are set out on page 42, and the responsibilities of the external auditors to the shareholders are set out on page 50.