



Report of the Chairman of the Supervisory Board
on the conditions governing the preparation and
organization of the Supervisory Board's work and
the internal control and risk management
procedures implemented by Vallourec

This document is prepared in accordance with legal obligations.
It is an extract of the Registered Document 2009.

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8.2 Report of the chairman of the Supervisory Board on the conditions governing the preparation and organization of the Supervisory Board's work and the internal control and risk management procedures implemented by Vallourec

In accordance with the provisions of Article L.225-68 of the French *Code de commerce*, the Chairman of Vallourec's Supervisory Board presents this report to the shareholders, detailing the conditions governing the preparation and organization of the Supervisory Board's work and the internal control and risk management procedures implemented by the Company.

In application of the law of 3 July 2008 incorporating EC directive 2006/46/EC of 14 June 2006, the AFEP-MEDEF corporate governance Code for listed companies of December 2008, resulting from the consolidation of the AFEP and MEDEF reports of October 2003 and their recommendations of January 2007 and October 2008 on the compensation of executive Corporate Officers of listed companies, is the Code with which Vallourec has decided to comply in the drawing up of the report provided for under Article L.225-68 of the French *Code de commerce*.

At its meeting on 6 April 2009, the Supervisory Board verified that the rules regarding remuneration and pensions applied by the Company to Management Board members complied with the AFEP-MEDEF Code. It approved, in particular, the terms of the contract appointing Philippe Crouzet as Chairman of the Management Board, having satisfied itself that said contract complies with the AFEP-MEDEF Code. These rules were, in accordance with the AFEP-MEDEF Code, published on Vallourec's website on 9 April 2009. The rules were supplemented on 10 August 2009 by an information document in connection with the incentive policy aimed at strengthening employees' stake in the results of the Vallourec Group and with the compensation policy relating to the allocation for 2009 of share options and performance shares to Management Board members.

This report was approved by the Supervisory Board at its meeting on 23 February 2010.

A – CONDITIONS GOVERNING THE PREPARATION AND ORGANIZATION OF THE SUPERVISORY BOARD'S WORK

The internal regulations of the Supervisory Board, the situation of Board members as regards the principles resulting from the AFEP-MEDEF Code and the composition and operation of the three Committees (Finance and Audit Committee, Appointments and Remuneration Committee and Strategy Committee) set up within the Supervisory Board are detailed in Section 6 of the Registered Document for the year ended 31 December 2009 dealing with corporate governance, which is an integral part of this report.

The number of meetings of the Board is normally set at four per year but additional meetings may be organized where circumstances so require. The Board met seven times in 2009. The average length of Board meetings is about three hours.

In order to ensure that Board members are able to attend meetings, the timetable of regular meetings is prepared very far in advance. The meetings timetable for 2009 was prepared at the Board meeting held on 31 July 2008. The meetings timetable for 2010, a preliminary version of which was presented to the Board at its meeting on 13 May 2009, was adopted by the Board at its meeting on 30 September 2009.

The effective attendance rate of Board members at meetings was higher than 80% on average for all the meetings held in 2009.

Dates of Board meetings (Financial year 2009)	Attendance rate
25 February	7/9 (78%)
6 April	7/8 (88%)
13 May	7/8 (88%)
3 June	7/9 (78%)
30 July	6/9 (67%)
30 September	7/9 (78%)
12 November	8/9 (89%)

Members who were unable to attend were, however, represented at all meetings, whether regular or exceptional. The members of the Management Board attended all meetings.

The arrangements for the meetings are confirmed on average a week in advance by means of a notice of the meeting to which is attached the agenda and the draft minutes of the previous meeting. Board members are invited to submit any comments they have in advance of Board meetings.

The Management Board circulates documents, in particular those of a financial nature, a few days in advance of Board Meetings, thereby enabling members to familiarize themselves with such documents before meetings. At meetings, a complete file incorporating the supporting documentation in respect of items on the agenda is given to each participant. This file also contains, in the case of meetings at which quarterly results are reviewed, the Management Board's quarterly report to the Supervisory Board on the Company's performance, prepared in accordance with the provisions of Article L.225-68, Section 4, of the French *Code de commerce*. Where necessary, the Board relies on preliminary work carried out by the Committees.

Meetings are chaired by the Supervisory Board Chairman who ensures, in particular, that each member expresses his opinion on the most important matters. In the unusual case of a Board member having a personal interest in one of the matters under consideration as specified in Article L.225-86 of the French *Code de commerce*, he will be required to leave the meeting while the matter concerned is being discussed.

In 2009, Vallourec's Statutory Auditors attended those Supervisory Board Meetings at which the annual and half-year financial statements were reviewed.

After the assessments of the operation of the Board carried out in 2003, 2006 and 2008, a further assessment was carried out in 2009 based on an updated version of the same questionnaire, which comprised six assessment topics. An analysis of the results, which was sent to Board members and discussed at a Board Meeting, shows a high level of satisfaction among all members. In the light of this summary, it was recommended and agreed that the composition of the Board be enlarged and that, where necessary, it be enlarged up to the statutory limit of 12 members to allow for, in particular, members who are women and/or have international stature or experience, or who may be of foreign nationality. The length of Board meetings, which increased during 2009, in accordance with the recommendation resulting from the assessment carried out in 2008, to allow for matters to be discussed in greater depth, appears to be appropriate overall, although some believe that three hours is a minimum. The quality of discussions was also assessed. The documentation presented as background information for these meetings is judged to be sufficiently detailed and constantly improving. Finally, Board members have expressed their support for continuing to visit employees on site once a year.

For the purposes of assessing the Group's performance, in 2009 the Supervisory Board focussed mainly on reviewing the annual and first half financial statements, the Group's activity, the results of the Cap Ten competitiveness plan, the strategic issues facing the Group and the projects and negotiations currently in progress.

As regards corporate governance, the Supervisory Board examined the following subjects in particular:

- the setting of the remuneration of the members of the Management Board and of its new Chairman;
- Vallourec's policy as regards remuneration and its incentive policy aimed at strengthening employees' stake in the results of the Vallourec Group, in particular as regards the measures adopted by the Management Board to ensure compliance with the provisions of law no. 2008-1258 of 3 December 2008 relating to employment income;
- the overall budgets and the number of performance shares and share subscription options allocated to each member of the Management Board, and the requirement for such members to retain a portion of the shares and options allocated;
- the payment of attendance fees to Supervisory Board members, Committee members and the Censeurs;
- the composition of the Supervisory Board following the appointment of Mr Philippe Crouzet as Chairman of the Management Board as from 1 April 2009 to replace Mr Pierre Verluca, and the resulting provisional appointment on 13 May 2009 of Mr Jean-François Cirelli as a member of the Supervisory Board.

B – SHAREHOLDER PARTICIPATION IN VALLOUREC'S SHAREHOLDERS' MEETINGS

Any shareholder is entitled to participate in the Company's Shareholders' Meetings in accordance with applicable laws and regulations and regardless of the number of shares held. Article 13 of the by-laws – which are available on the Company's website http://www.vallourec.com/download.asp?url=pub/assemblee_generale_fr/155_A.pdf and at the registered office – relating to Shareholders' Meetings does not stipulate any specific procedures for participation, it being specified, however, that "Holders of shares with regard to which not all payments due have been paid within 30 days as from formal notice being given by the Company shall not be allowed to attend Shareholders' Meetings. These shares shall be deducted in the calculation of the quorum".

Since Vallourec places great importance on the attention paid to its shareholders, it endeavours, whenever it can, to improve shareholder participation at its Shareholders' Meetings, by making shareholders aware of such Meetings in advance, by publishing informa-

tion over and above that required by law in specialist newspapers and by sending a shareholders' letter to all of them in the weeks preceding each Annual Shareholders' Meeting.

The list of attendees at the Ordinary and Extraordinary Shareholders' Meeting held on 4 June 2009 shows that 1,677 shareholders were present, represented or voted by correspondence; they owned 26,293,488 shares out of a total of 53,788,716 (48.88%) and 26,339,066 voting rights out of a total of 53,495,793 (49.23%), resulting in a quorum increased by 5%. The attendees included the Bolloré group, which owned 2,990,534 shares representing the same number of voting rights, i.e. 5.56% of the capital represented and 5.55% of the voting rights exercised.

Vallourec's policy as regards shareholder information and information concerning the structure of the Company's capital and the factors likely to have an impact in the event of a takeover bid are detailed in Section 2 of the 2009 Registered Document, as required under the provisions of Article L.225-100-3 of the French *Code de commerce*.

C – INTERNAL CONTROL AND RISK MANAGEMENT PROCEDURES

1. Objectives of internal control

The Group's internal control system was developed and implemented with significant involvement from the Group's staff. It aims to provide reasonable assurance that the following four objectives may be achieved:

- compliance with laws and regulations in force;
- proper application of the instructions issued and compliance with the policies laid down by the Management Board;
- proper operation of internal processes (in particular those relating to the safeguarding of assets); and
- accuracy of financial information.

In contributing to the effectiveness of its operations, the efficient use of its resources and the control of risk, this internal control system plays a key role in the management and supervision of the Group's various activities. As is the case with any control system, the Group's internal control system cannot provide an absolute guarantee that the Group's objectives will be achieved and that all risk of error or fraud is fully eliminated or controlled

2. Components of internal control

To guarantee the consistency of day-to-day procedures carried out worldwide in the Group's name, in 2009 Vallourec implemented a group of procedures which constitute the basis of the internal rules applicable to all its staff and departments.

Situated at the heart of Vallourec's internal control system, these procedures provide a framework for the actions of each employee. They relate, in particular, to ethics, the delegation of authority, the confidentiality of information, the prevention of insider trading, external communication and financial communication.

The Code of Ethics

The Group's ethical standards have, since 2009, been set out in a single document: the Code of Ethics.

The Code of Ethics is based on a set of fundamental values, such as integrity and transparency, standards and professionalism, performance and responsiveness, respect for men and women and joint commitment.

It provides a frame of reference for the proper conduct of the day-to-day activities of each employee by means of principles for action, which are based on the aforementioned values. These principles for action reflect the way in which Vallourec means to conduct its relations with all partners and other parties, such as employees, its customers, shareholders and suppliers and constitute a benchmark for the Group, especially in implementing its sustainable, responsible development plans.

The Code of Ethics also prescribes rules of conduct on a variety of subjects, such as conflicts of interests, relations with third parties and the conservation of assets in such a way as to protect, under all circumstances, the Group's reputation and image.

Vallourec's Code of Ethics applies to all Group consolidated companies. Each employee is personally responsible for implementing its values and principles and complying with rules Vallourec publishes.

Management makes the Code of Ethics known to all Group personnel. It has been translated into five languages. It has also been published on the Company's website http://www.vallourec.com/download.asp?url=pub/publication_uk/39_P.pdf – to affirm the Group's values with regard to third parties.

In order to support implementation of the Code of Ethics by all Vallourec personnel, in particular managers, a Code of Ethics officer has been appointed for the Group, whose duties are:

- to assist Group companies in disseminating the Code of Ethics;
- to coordinate actions to make new employees aware of the Code of Ethics;
- to participate in setting procedures for applying the Code;
- to ascertain any difficulties in interpreting or applying the Code of Ethics that are raised by staff; to that end, the officer receives any information relative to breaches of the principles of responsibility;
- to produce an annual report on implementation of the Code of Ethics for the Chairman of the Management Board.

The Code of Ethics officer reports to the Management Board and relies on a network of local contacts.

Delegated authority procedure

The level of authority given to each manager within the Group must remain compatible with the maintenance of an overall level of control, the Group's strategy and the application of rules common to all Group entities.

To better meet these requirements, the aim, at Group level, of the delegated authority procedure implemented in 2009 is to define clearly the approval levels which must be complied with before commitments can be entered into by any Group entity. It may not constitute a departure from the prevailing legislation and regulations.

Confidentiality Charter

Against a backdrop of intense competition, the Group has needed to make all staff aware of their obligations as regards confidentiality. Vallourec therefore drew up a confidentiality charter with the aim, on the one hand, of enabling it to carry out its business in better conditions when faced with such competition and, on the other hand, of protecting people working for Vallourec by informing them as accurately as possible of the duty of confidentiality with which they must comply.

The Code of good practice on transactions in Vallourec shares

Vallourec has a Code of good practice on the prevention of insider trading that could occur in connection with transactions in its shares.

This Code concerns not only all the members of its management and control bodies, but also all senior managers and employees of Vallourec and all its subsidiaries. It is sent to all employees who come into possession of insider knowledge, of whom the Companies maintains an up-to-date list.

Its objective is to ensure compliance with the precautionary principle in order to (i) protect staff at all levels by making them aware of stock exchange regulations and applicable penalties, so as to enable them to avoid being the subject of legal proceedings, (ii) protect Vallourec and its Group, in particular from the risks of damage to its image and reputation and a fall in the value of its shares, and (iii) retain the confidence of investors and maintain equality between shareholders.

External communication procedure

Vallourec has drawn up an external communication procedure, the aim of which is to ensure the consistency of information provided to the outside world (oral and written), which may affect Vallourec's reputation (social, environmental, etc.).

Any information communicated outside the Group relating, in particular, to the order book, new contracts, capital expenditure, planned acquisitions or more generally the Group's past or future activity must be the subject of an internal approval process.

The financial communication procedure

In 2009, Vallourec drew up a financial communication procedure, the aim of which is to ensure that the Group's system of providing financial information to the public complies with the prevailing legislation and regulations.

Annual and half-year financial reports and quarterly financial information is thus the subject of an internal approval process prior to its release and filing with the French securities regulator (*Autorité des Marchés Financiers* – AMF).

3. Description of internal control procedures

3.1 INTERNAL CONTROL PROCEDURES ADAPTED TO THE SPECIFIC CHARACTERISTICS OF VALLOUREC

Responsibility for implementing appropriate internal control procedures governing risk management, financial control and compliance with legislation is delegated to the managers of each Group company.

To ensure the consistency of Group procedures worldwide, senior management relies on the functional departments to draw up the procedures necessary for the proper operation of controls, issue instructions regarding their implementation and ensure compliance with said instructions.

In accordance with Article L.823-19 of the French *Code de commerce*, the Finance and Audit Committee monitors the financial information preparation process and the effectiveness of the internal control and risk management systems.

The Group's key operations and the control procedures applicable to them are as follows.

3.2 INTERNAL CONTROL PROCEDURES IN RESPECT OF FINANCIAL AND ACCOUNTING INFORMATION

3.2.1 Financial and accounting reporting

Financial and accounting information is prepared centrally on the basis of the subsidiaries' financial statements, adjusted to comply with Group standards. The necessary data is collected and processed by means of a reporting and consolidation software application that is used by all consolidated subsidiaries and is compatible with the IFRS accounting standards that Vallourec adopted on 1 January 2005.

Reports are produced monthly in the month following the end of the month to which they relate whereas full accounting consolidations are produced quarterly within two months following the end of the quarter to which they relate. The monitoring of off-balance-sheet commitments is an integral part of the quarterly consolidation process.

3.2.2 External financial information

Since 2007, the Company has released quarterly information as at 31 March and 30 September including, in particular, the consolidated balance sheet and income statement. The preparation of the quarterly, half-yearly and annual consolidations is the responsibility of the Management Board. The annual financial statements are audited and the half-year financial statements are reviewed by the Statutory Auditors; quarterly data is neither audited nor reviewed.

3.2.3 Cash position and financing

Responsibility for cash management is delegated to individual companies, by means of well-defined procedures and delegation of authority. Any departure from the general rules requires the prior authorization of the Group Finance department.

The Group Finance department is also responsible for borrowings and investments with a term of more than one year. Responsibility for borrowings and investments with a term of less than one year is delegated to the subsidiaries, which are required to comply with specific Group procedures: quality of the banks involved, risk-free investment and monitoring of financial guarantees given.

Transactions in foreign currencies and foreign exchange hedging are also governed by rules issued by the Group Finance department.

In 2007, the Group centralized the euro and US dollar cash management for its main European companies and the currency hedging operations in respect of its US dollar sales. This system contributed to better cash management and the security of market transactions.

Subsidiaries' borrowings, investments and foreign exchange transactions are monitored on a monthly basis by means of a report produced by the Head of Group Treasury and submitted to the Management Board.

3.2.4 Procedures and instructions

With the objective of producing high-quality financial and accounting information, Vallourec has produced procedures and instructions tailored to the French and foreign subsidiaries. These procedures are classified by topic and deal mainly with accounting, treasury and reporting issues and with the IFRS framework.

Details of the procedures are available on an intranet site that can be consulted by all of the Group's finance staff.

In 2008, all fully-consolidated companies carried out a self-assessment review of their accounting and financial procedures on the basis of a questionnaire comprising 121 questions. The questionnaire was based on the report of the COSO (Committee of Sponsoring Organizations of the Treadway Commission) and complies with the provisions of the application guide for the frame of reference of the French securities regulator (*Autorité des marchés financiers* – AMF) relating to the internal control of financial and accounting information published by issuers.

In 2009, all these companies were the subject of an on-site review by the Internal Audit department on the basis of this questionnaire. The review covered the following financial and accounting cycles: capital expenditure, purchasing, inventories, sales, cash, provisions, staff, taxes and reporting processes. Each company received a summary in 2009 of the points for improvement and prepared an action plan for each weakness identified in respect of which the risk of occurrence and the potential impact on the financial statements was considered to be significant.

3.2.5 Internal audit

The Internal Audit and Financial Control department reports to the Group Finance department. It audits the subsidiaries in accordance with an audit plan designed to assess and improve the accuracy and reliability of accounting and financial information.

In addition to the team based at the Group's head office, Vallourec has an auditor based at V & M Deutschland and a team based at V & M do Brasil. The team's audit plans are validated by the Internal Audit department. Its responsibilities relate mainly to internal control procedures.

External consultants may be used in the case of one-off assignments.

The Internal Audit department also coordinates relations with the Statutory Auditors, who are mainly affiliated with international audit firms.

3.3 OTHER KEY PROCESSES ANALYZED

3.3.1 Industrial investment

The Technology and Investment department, grouped since 1 January 2010 with the Research and Development department within a single department (the Technology, R & D and Innovation department) reports to a member of the Management Board and to an Investments Committee composed of members of the Executive Committee, the Management Control department and the Corporate Investment department.

This Committee meets six times a year. It examines budgets, expenses for the period and, where relevant, deferred expenses. The agenda comprises a review of projects with a forecast cost of more than €5 million or less than this amount when they are strategic in nature. In accordance with the Large Capex Approval procedure, a file is prepared in respect of these projects by the division concerned and a memorandum drawn up by the Management Control department before the projects are submitted for approval to the Management Board, in accordance with the Delegated Authority procedure detailed on page 221.

A posteriori controls are carried out on expenses, expected objectives and the profitability of capital expenditure projects. Such controls are performed by the Technology and Investments department or the Management Control department on projects that are deemed highly representative, which were authorized in earlier years and which involve mass production. In addition, project management audits may be carried out during the project implementation phase by the Group Quality department. The results of these audits are brought to the attention of the divisions and Investments Committee.

3.3.2 Quality – Safety – Environment

The QSE (Quality, Safety and Environment) department defines the systems, methods and tools used in the Group, in accordance with the requirements of quality management (standards ISO 9001 and ISO/TS 16949, API, ASME, etc.), health and safety (OHSAS 18001 standards) and environmental standards (ISO 14001).

These elements form the Vallourec Management System (VMS), which has been implemented in all Group companies. The VMS has been structured around three main components:

- Total Quality Management (TQM) plans, i.e. plans for monitoring the Group's entities, which facilitate the control of processes by identifying operational performance measurement indicators;
- the Continuous Improvement Teams (CIT), which promote the commitment of staff to continuous improvement in accordance with the same operational indicators, by implementing a stringent, standardized method for resolving problems;
- the steering committees, which ensure the commitment of senior management, and the monitoring and support of the continuous improvement approach.

In addition to the control of processes and continuous improvement, the VMS is responsible for ensuring that initiatives are consistent with the aims of the strategic plan.

The QSE department is responsible for the continuous auditing of the VMS in all Group entities, identifying variances and areas with room for improvement, issuing recommendations and ensuring they are taken into account in the action plans. This work is carried out in collaboration with the external certification bodies and with the internal departments involved, in particular the Human Resources department and the Management Control department.

- As regards quality, the QSE department is responsible, in the context of the VMS, for applying specific methods and tools designed for the continuous improvement of the quality of the Group's products and control of its manufacturing processes. It assists with their implementation, sets up the necessary training programmes and oversees the sharing of best practice. By means of the audits it carries out at all Group sites, in addition to those carried out by external certification bodies, it ensures said practices are properly applied to all processes which contribute to customer satisfaction.

The Vallourec Quality approach takes into account the requirements of the most stringent standards, in particular as regards standardization, the control of variations in quality, risk prevention and problem resolution.

- As regards safety, in 2008 the Group launched the Cap Ten Safe project, the aim of which is to significantly enhance our performance in this area. It illustrates the Group's intention to make a complete break with the past and to carry out an extensive overhaul of all safety measures with the aim of achieving continuous, ongoing improvements in the Group's safety culture.

This plan is in line with the VMS and consistent with the following three fundamental principles: the commitment of all senior management, the involvement of all staff and the implementation of appropriate monitoring indicators.

It comprises, in respect of the period 2009-2010, the following main initiatives:

- improving performance at all plants to ensure compliance with Vallourec standards, particularly in the areas of risk evaluation, monitoring, control and updating of safety initiatives and order and cleanliness of the shop floor;
 - building a safety management system: Vallourec intends to gain OHSAS 18001 certification for its main industrial sites during the 2009-2010 period;
 - fostering a genuine safety culture: at the end of 2008, the Group launched a programme under which all plant staff would receive a safety visit. These visits, which took place throughout 2009, would involve observing an operator at his place of work, followed by dialogue, the aim of which is to make staff aware of safety behaviour. The objective is to carry out two visits per employee per year;
 - the Cap Ten Safe project has enabled the Group to achieve significantly improved safety performance as from 2009: the accident frequency rate (or Lost Time Injury Rate – LTIR) decreased, for the entire Group, from 9.2 in 2008 to 5.3 in 2009.
- As regards the environment, the QSE department is responsible for coordinating and directing environmental matters and relies on local environment managers who are responsible for ensuring compliance with regulations and improving Group performance in the field of environmental protection in accordance with the sustainable development charter drawn up by the Group in 2004.

It carries out audits and establishes key indicators that enable the main parameters to be periodically monitored.

The environment report is published annually. It describes the environmental situation and the progress achieved at all Vallourec sites.

Vallourec's main sites, which account for more than 98% of the Group's production, now have certification under ISO 14001. There are a few relatively small sites for which the Group plans to obtain certification in 2010.

The aim of the GreenHouse project, launched in 2009, is to draw up and implement initiatives designed to prepare the Group for the "carbon economy" and thereby to integrate its efforts to combat global warming into its strategic decisions. The objective is to significantly reduce the consumption of energy (gas and electricity) and therefore greenhouse gas emissions. The QSE department is responsible for coordinating these initiatives.

Finally, the Group has continued to make significant investment in the field of environmental protection and safety. In 2009, investment in these fields represented around 7% of the Group's total capital expenditure.

3.3.3 Research and Development

The Research and Development department, which has since 1 January 2010 been grouped with the Technology and Investment department within the Technology, R & D and Innovation department, as described on page 43 above, has drawn up procedures at Group level concerning the management of programmes for developing new products and industrial processes. The processes thus defined are applied in a consistent manner by the entities concerned, particularly as regards intellectual property.

Training and specific assistance by experienced professionals were introduced in respect of certain selected projects. The divisions' project portfolios are monitored on the basis, in particular, of their potential benefit to the Group and the risks that might be incurred.

Each year, audits are also carried out by the Group Quality department in accordance with the VMS.

3.3.4 Purchasing

In 2009, the Purchasing department quickly adapted to the economic crisis by expanding its principal annual objectives for priority action.

The Group focussed on three additional initiatives:

- renegotiating all annual and long-term contracts against a backdrop of falling activity levels;
- ensuring the financial security of and monitoring of the Group's strategic suppliers;
- rapidly adapting volumes purchased on the basis of orders placed by Group employees.

These initiatives enabled the Purchasing department to meet, in 2009, the contribution targets set by the Cap Ten Safe project.

The Group continued in 2009 the actions taken in 2008 to improve the structure of the purchasing function. As a result, the involvement of the Purchasing department in the areas of raw materials and capital expenditure resulted in significant gains for the Group.

3.3.5 Information systems

In 2009, the Group continued to implement the programme of IT security audits initiated in 2008, as a result of which corrective action has been taken. In particular, a contract was entered into for the hosting by a third party of the Saint-Saulve IT centre, housing the French application servers and certain services at Group level. Migration is in progress and will be completed in May 2010. As a result, the Group will be able to eliminate the risk of the IT centre being out of action since these new arrangements will guarantee that it is permanently operational.

Several initiatives were implemented in 2009 to improve the Group's IT security:

- the first phase of the project for the segregation of access rights (segregation of duties) to IT applications was completed (GRC project);
- the Group continued with the deployment of the SAP core model in the United States via VAM USA. The system is scheduled to become fully operational during 2010;
- a global contract was signed with an anti-virus software provider for the use of one single system throughout the Group;
- the architecture was defined for a new distance connection solution for Vallourec's staff and partners, the aim of which is to strengthen the security of communication. It will be deployed gradually as from 2010;
- finally, a project was launched to make uniform and strengthen the management of access to the Group's information system. The new architecture will be deployed in 2010 and early 2011.

3.3.6 Human Resources

In 2009, the Human Resources department introduced an internal control process which audits all its operations: the performance of its duties, training and skills management, the working environment, compliance with the Group's internal regulations and the prevailing national labour regulations, compensation management and the protection of privacy and information regarding the Company and its employees.

Each country with its own Human Resources department carries out a self-assessment review of its operations using a standardized questionnaire. On the basis of the answers received, the Group Human Resources department carries out audits and monitors plans for corrective action or improvements. In 2009, the main countries in which the Group operates completed the self-assessment questionnaire and were audited on the basis of their replies. The countries concerned were Brazil, France, Germany, the United States, China, the United Kingdom, Mexico and the United Arab Emirates.

The same type of assessment is also used in respect of the acquisition and integration of new Group companies.

This approach also enables best practice to be identified and implemented on a Group-wide basis.

As regards the prevention of industrial accidents and sickness, the Group-wide Cap Ten Safe programme (see 3.3.2 above), which was launched in 2008, is enabling the Group, by aiming to obtain OHSAS 18001 certification, to focus on generalized and standardized safety management in all plants. It relies on significant commitment on the part of the Group's senior management and the involvement of all staff.

In 2009, the Group significantly reduced the number of accidents and the resulting number of working days lost.

3.3.7 Customer relations

With the aim of specifying and formalizing certain practices regarding contractual relations with its customers, Vallourec has developed a procedure for managing customer risk through limits in respect of credit and delegation of authority and credit insurance. In the same

spirit, general sales terms have been drawn up to be applied by all Group entities, with the aim of making practices consistent throughout the Group and reducing risk exposure.

The Legal department periodically analyzes the legal provisions applicable to sales contracts entered into between the subsidiaries and their customers. General terms, standard documents, sales contracts and bids in response to invitations to tender are reviewed on a regular basis.

3.3.8 Insurance

Industrial risks are covered by two types of Group insurance: general insurance (direct material damage to Group property, not subject to specific exclusions, as well as any costs and resulting losses) and third-party liability insurance (liability arising as a result of injury or loss caused to third parties either resulting from the Group's operations or after delivery of goods or services).

4. Risk management

Risks are managed by the industrial and sales units and by the functional departments (Finance, Human Resources, Legal, Purchasing, Quality, IT, Insurance, etc.). In addition, Vallourec is developing a Group-wide policy to ensure that risk management is consistent, comprehensive and well-monitored.

Vallourec's Risk Manager coordinates a top-down approach, which involves the entity's principal managers evaluating the major risks in order to implement measures to reduce the probability and impact of such risks. The method establishes priorities according to the Group's projects, by taking into account the "potential for improvement" of controls. Therefore, a "major" risk, for which Vallourec already has a control in place on a par with the best practice in the industry (prevention, protection against the consequences and insurance), will simply remain under surveillance. However, a "high" risk, for which Vallourec has not yet optimized its controls, will result in the drawing up of an action plan.

Risk mapping is in place for each of Vallourec's divisions and at Group level as regards the provision of information to the Management Board. Each describes the main risks, their scenarios, past occurrences, the controls in place, and, where applicable, the best control practices of other companies. It is therefore these main risks that justify the launching of action plans.

Vallourec's divisions and Management Board manage their risk mapping by means of a committee that meets each half year. Vallourec's Risk Manager attends the committee meetings in order to stimulate discussion, guarantee the consistency of the action taken and report to the Management Board. All committee meetings are attended by the division's manager and his main assistants. The functional managers affected by certain risks are also invited to attend (e.g., R & D and IT). Each committee meeting handles the following matters:

- validation and monitoring of action plans, presented by the owner of each priority risk;
- validation of the key risk indicators which will guarantee the relevance of new controls, after closure of the action plan, and their long-term survival;
- updating of the self-assessment of priority risks.

Therefore, on a regular basis since the establishment of the risk mappings in 2007, control over the priority risks has been increased to the level of the industry's best practice. Risk Management is being integrated into the Vallourec Management System via its systematic practice of committee meetings and management indicators. The risk management function serves as a supplement to the Group's internal control and internal audit functions. It collaborates with them and helps to draw up the internal audit programme. It methodically tests the efficacy of the internal control procedures referred to above and then elevates them to the level of best practice. As a result, specific procedures have been implemented to ensure the prevention of:

- physical risk to an employee in the performance of his duties;
- the risk of the disclosure of confidential information ;
- the risk of media attention not under the Group's control.

Additional cover has been taken out at Group level or by certain subsidiaries against a number of other insurable risks.

In conclusion, risk management is based on internal control that is becoming increasingly comprehensive and tailored to the Group's specific requirements, with the result that it assists in the development of said internal control by anticipating risks, benchmarking procedures and managing action plans at the highest level within the divisions and Management Board.

Additional information is provided in Section 4, paragraph 4.2 "Risk management".

D – PRINCIPLES AND RULES FOR DETERMINING THE REMUNERATION OF CORPORATE OFFICERS

1. Remuneration of Management Board members

The general principles of the Management Board remuneration policy and an analysis of the individual position of each of its members are presented to the Supervisory Board by the Appointments and Remuneration Committee, which bases its recommendations on research and advice from a leading international firm specializing in management and Corporate Officer remuneration.

A breakdown of the remuneration of the Group's Corporate officers is provided in Section 6 of the 2009 Registered Document dealing with Corporate Governance, which is an integral part of this report.

The monetary remuneration of Management Board members is composed of a fixed portion and a variable portion. Their remuneration is compared each year to a reference sample made up of listed French industrial groups, Vallourec's policy being to maintain the fixed and variable portions at or below the respective medians of this sample.

Two-thirds of the variable portion is based on the Group's consolidated net profit and one-third is based on the achievement of individual targets set by the Supervisory Board. The variable portion may not exceed 90% of the fixed portion in the case of the Chairman of the Management Board and 75% in the case of other Management Board members. The basis for calculating the Group's consolidated net profit is verified by the Statutory Auditors.

At its meeting on 23 February 2010, the Board decided that, in 2010, the variable portion of Management Board members' remuneration would be calculated in thirds, the first third being based on the net profit, the second on EBITDA and the third on the achievement of targets set by the Board. The basis for calculating the first two thirds will be verified by the Statutory Auditors.

In order to enable them to obtain an interest in the Group's capital, Management Board members may be granted share subscription or share purchase options and performance shares under the conditions drawn up by the Supervisory Board, based on the recommendations of the Appointments and Remuneration Committee. Since 2006, all allocations of performance shares have been subject to the Group achieving a target EBITDA/sales ratio. The same applies to a significant portion of the share subscription options granted to Management Board members in 2008 and to all option granted to them since 2009.

Since 2007, and in accordance with the AFEP-MEDEF Code, Management Board members have been required to retain until the end of their terms of office, (i) one quarter of the performance shares granted to them under the terms of a plan, and (ii) the equivalent in Vallourec shares of one quarter of the gross capital gain realized on the date of sale of the shares resulting from the exercise of options. Management Board members formally undertake not to use hedging instruments in connection with the exercise of options, the sale of shares resulting from the exercise of options or the sale of performance shares.

As regards pension provision, Management Board members, like all the Group's senior management, are covered by a supplementary pension scheme that complies with the AFEP-MEDEF Code. The terms and conditions applicable to this supplementary pension scheme are detailed in the section of the management report dealing with regulated agreements and commitments. Beneficiaries may retain their benefits under the scheme if they are dismissed on or after their 55th birthday and are unable to find alternative employment.

This scheme, which does not give any specific benefits to Management Board members over and above those applicable generally to the Group's senior management, appears reasonable since the additional pension is capped at 20% of the average base salary, excluding the variable portion, for the last three years and limited to four times the annual social security ceiling. The gross theoretical annuity is equal to the sum of the annual rights calculated in respect of each full financial year in accordance with the following formula: $C = 0.25 \times (B/P) - 1^{(1)}$.

The new Chairman of the Management Board, whose term of office commenced on 1 April 2009, does not have an employment contract with the Group. He is entitled to a termination payment in the event that his departure is imposed on him and in the event of a significant change in the Group's capital structure, a merger or a change of strategy initiated by the Supervisory Board or the Company's shareholders. In accordance with Article L.225-90-1 of the French *Code de commerce* and the AFEP-MEDEF Code, the receipt of such payments would be conditional upon performance requirements. The amount of such payments may not exceed twice the gross annual monetary remuneration. Were he to leave the Company under the same circumstances and before exercising the share subscription or share purchase options granted to him, the Chairman of the Management Board would still be entitled to them, subject to the performance requirements.

⁽¹⁾ $C = \text{Annual rights capped at 2\%}$
 $B = \text{Annual base salary}$
 $P = \text{Annual social security ceiling}$

The other members of the Management Board are not entitled to any termination payments if they are dismissed by the Company. Those who had employment contracts with Vallourec & Mannesmann Tubes before they were appointed as members of the Company's Management Board, application of which is suspended during their term of office, are entitled to a redundancy payment in the event that they are dismissed by Vallourec & Mannesmann Tubes. The amount of such redundancy payment is equal to two years' gross fixed remuneration in respect of said contract of employment, plus a lump sum variable amount of 12.5%.

2. Remuneration of supervisory board members

The maximum annual attendance fees for allocation by the Supervisory Board to its members were increased to €400,000 by the Ordinary Shareholders' Meeting of 1 June 2006 (*Fifteenth resolution*).

From 2007 until 2008, each Board member and each *Censeur* received attendance fees set at €28,000 per year, reduced pro rata in the case of an appointment or termination of an appointment during the year.

To ensure that it complies with the provisions of Article 18 of the AFEP-MEDEF Code and the practice of most CAC 40 companies, which allocate all or part of their attendance fees on the basis of members' attendance at meetings, the Supervisory Board, in accordance with the recommendation made to it by the Appointments and Remuneration Committee, decided to adopt a new procedure as regards the remuneration of Board members: the aforementioned €28,000 total is now divided into two equal fractions, one of which will be paid in full and the other allocated on the basis of members' attendance at meetings. This new rule has been applied since 1 July 2009.

The Chairman of the Supervisory Board receives remuneration, the amount of which was increased by the Supervisory Board, as recommended by the Appointments and Remuneration Committee, to €250,000 per year with effect from 1 January 2006. He also receives attendance fees of €28,000. The Chairman and members of the Supervisory Board were not awarded any share options, performance shares or termination payments of any kind.

3. Remuneration of Committee members

Members of the Committees (Finance and Audit Committee, Appointments and Remuneration Committee and Strategy Committee) receive, as part of the aforementioned €400,000 annual budget, additional attendance fees based on their actual attendance at meetings of said Committees, at the rate of €2,500 per meeting. Committee Chairmen receive €3,500 per meeting, with the exception of the Chairman of the Appointments and Remuneration Committee, who has waived his right to receive remuneration in his capacity as Chairman of said Committee.

4. Remuneration of the Censeurs

Remuneration of the Censeurs comes within the annual budget for attendance fees allocated to the Supervisory Board.

5. Corporate Governance

The Supervisory Board has decided to adopt the AFEP-MEDEF Code, as amended for application to limited companies managed by a Supervisory Board and a Management Board. The Code may be consulted on the AFEP-MEDEF website.

Vallourec has applied the recommendations of the Code.

In view of the above, Vallourec believes that it complies with the corporate governance regulations currently in force in France.

8.6.4 Statutory Auditors' report, prepared in accordance with Article L. 225-235 of French *Code de commerce* on the report prepared by the Chairman of the Supervisory Board of Vallourec

This is a free translation into English of the Statutory Auditors' report issued in French prepared in accordance with Article L.225-235 of French Code de commerce on the report prepared by the Chairman the Supervisory Board on the internal control and risk management procedures relating to the preparation and processing of accounting and financial information issued in French and is provided solely for the convenience of English speaking users.

This report should be read in conjunction and construed in accordance with French law and the relevant professional standards applicable in France.

Year ended 31 December 2009

To the Shareholders,

In our capacity as Statutory Auditors of Vallourec and in accordance with Article L.225-235 of French *Code de commerce*, we hereby report on the report prepared by the Chairman of the Supervisory Board of your Company in accordance L.225-68 of French *Code de commerce* for the year ended 31 December 2009.

It is the Chairman's responsibility to prepare, and submit to the Supervisory Board for approval, a report on the internal control and risk management procedures implemented by the Company and containing the other disclosures required by Article L.225-68 of French *Code de commerce*, particularly in terms of corporate governance.

It is our responsibility:

- to report to you on the information contained in the Chairman's report in respect of the internal control and risk management procedures relating to the preparation and processing of the accounting and financial information; and
- to attest that this report contains the other disclosures required by Article L.225-68 of French *Code de commerce*, it being specified that we are not responsible for verifying the fairness of these disclosures.

We conducted our work in accordance with professional standards applicable in France.

INFORMATION ON THE INTERNAL CONTROL AND RISK MANAGEMENT PROCEDURES RELATING TO THE PREPARATION AND PROCESSING OF ACCOUNTING AND FINANCIAL INFORMATION

The professional standards require that we perform the necessary procedures to assess the fairness of the information provided in the Chairman's report in respect of the internal control and risk management procedures relating to the preparation and processing of the accounting and financial information. These procedures consisted mainly in:

- obtaining an understanding of the internal control and risk management procedures relating to the preparation and processing of the accounting and financial information on which the information presented in the Chairman's report is based and the existing documentation;
- obtaining an understanding of the work involved in the preparation of this information and the existing documentation;
- determining if any significant weaknesses in the internal control procedures relating to the preparation and processing of the accounting and financial information that we would have noted in the course of our engagement are properly disclosed in the Chairman's report.

On the basis of our work, we have nothing to report on the information in respect of the Company's internal control and risk management procedures relating to the preparation and processing of accounting and financial information contained in the report prepared by the Chairman of the Supervisory Board in accordance with Article L.225-68 of French *Code de commerce*.

OTHER DISCLOSURES

We hereby attest that the Chairman's report includes the other disclosures required by Article L.225-68 of French *Code de commerce*.

Paris La Défense and Neuilly-sur-Seine, 16 April 2010

The Statutory Auditors

KPMG Audit

Deloitte & Associés

Department of KPMG SA

Jean-Paul Vellutini

Philippe Grandclerc

Jean-Paul Picard

Jean-Marc Lumet



French limited liability company
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Supervisory Boards
and issued capital of € 229,123,156

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