Transparency in reporting

A comparison of reporting by private equity owned portfolio companies and listed companies

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Summary

In February 2007, The British Private Equity and Venture Capital Association (the "BVCA") asked Sir David Walker to undertake an independent review of the adequacy of disclosure and transparency in private equity, with a view to recommending a set of voluntary guidelines for the industry. This review resulted in the Guidelines for Disclosure and Transparency in Private Equity published in November 2007 ("the Walker Guidelines"). These Guidelines require additional disclosure and communication by private equity firms and relevant larger portfolio companies.

The UK private equity industry has embraced the Walker Guidelines. This has been an important step in increasing transparency. More than 60 portfolio companies have provided additional disclosures through information on their websites and through financial and narrative reporting.

This report, put together at the request of the BVCA, compares reporting by portfolio companies subject to the Walker Guidelines (the "Walker companies"), with companies in the FTSE 350. The analysis that underpins this report assesses the disclosures made in the annual report and accounts of each company in terms of ten data points. This enables a meaningful comparison to be made.

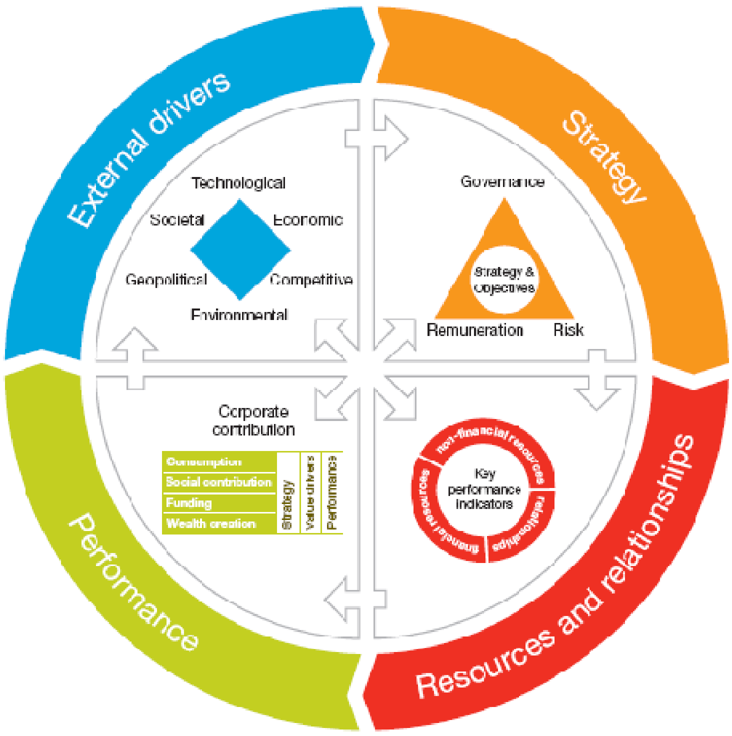
The effect of the Walker Guidelines has been to move reporting and disclosure by these portfolio companies towards the scope and quality of reporting of listed companies.

The analysis in this report shows that the Walker companies report to a standard that is generally consistent with reporting by FTSE 350 companies and, in places, better than FTSE 350 companies. Compared with the FTSE 350, Walker companies could enhance their disclosures in respect of strategic priorities. However when they do so, they are more likely to use the strategy to underpin their overall reporting than FTSE 350 companies.

What we looked for

For each company, PricewaterhouseCoopers LLP (UK) assessed the effectiveness of their communications using the following focus areas to consider the relevant aspects of corporate and narrative reporting:

One information set



The analysis in this report assesses the disclosures in corporate and narrative reporting for each company in terms of:

- the communication of the company's strategy including the overall governance and remuneration arrangements and the risks faced by the company as well as how these risks are managed;
- the resources and relationships that are key to the company's business;
- the assessment of the company's performance in terms of both financial and non-financial measures; and
- the external drivers impacting the company.

What we reviewed

We carried out a desk top review of the accounts of each of companies included in the analysis. We obtained the accounts from the websites of these companies and did not contact any of the companies. The data is based on the results of the work undertaken in 2009 to review the narrative reporting sections of the annual reports of the Walker companies and the FTSE 350. We looked at reports for years ended between 1 April 2008 and 31 March 2009. Four portfolio companies and six FTSE 350 companies were not reviewed because they did not report in this period. The final sample size was therefore 58 portfolio companies as compared to 344 companies comprising the FTSE 350 index.

We examined the contents of the report and accounts to assess whether they included the disclosures on the following ten data points:

- disclosure of key financial and non-financial performance indicators ("KPIs");
- disclosure of principal risks and uncertainties;
- outlining of strategic priorities;
- providing detail on cash flow / funding strategy;
- providing information on future trends and factors;
- using strategy to underpin their reporting;
- aligning remuneration with strategy and KPIs;
- clearly aligning KPIs and strategy;
- aligning sustainability with strategy; and
- providing information on contractual arrangements.

The results of this analysis are shown on the following pages.

Trends in corporate/narrative reporting - comparison to FTSE 350

We set out below a summary comparing the corporate/ narrative reporting practices of the portfolio companies complying with the Walker Guidelines and the listed companies comprising the FTSE 350 based on the ten data points we have collated.

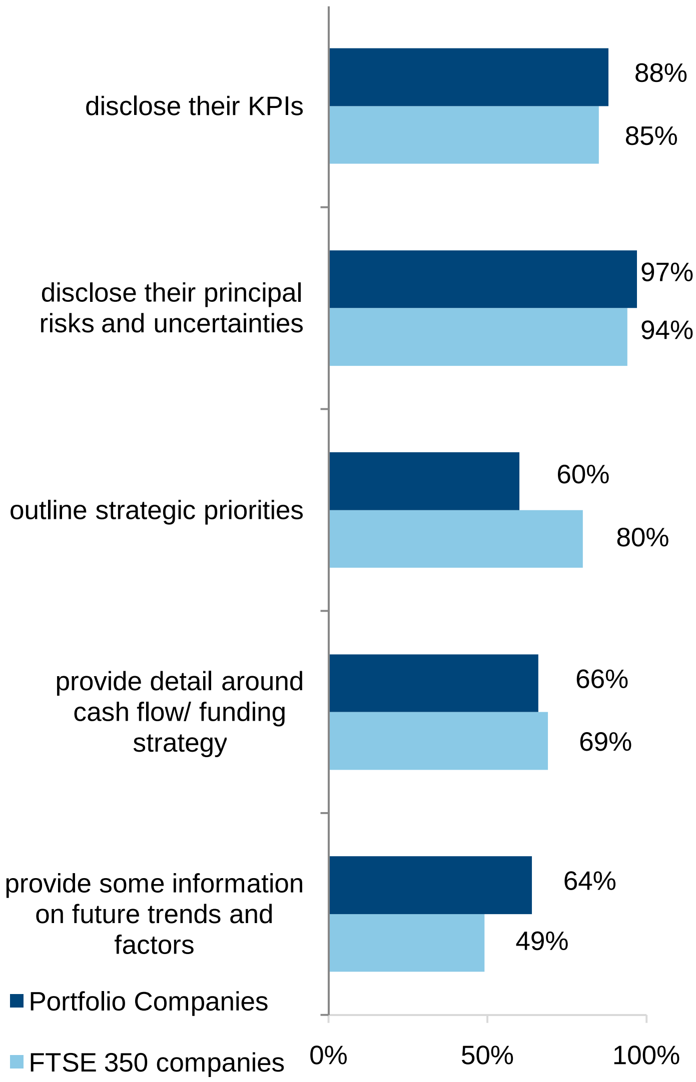
Disclosures of key performance indicators (typically financial) and principal risk and uncertainties are a strong area for both the FTSE 350 and portfolio companies considering that this is a mandatory disclosure under company law.

Disclosure of principal risks and uncertainties is an area of strong compliance by both sets of populations.

Outlining the key strategic priorities is an area where portfolio companies trail FTSE 350. This may be reflective of the different shareholder base and the requirements the analyst community have from listed companies. This is the most significant difference between reporting by portfolio companies and the FTSE 350.

Around 70% of the portfolio companies and the FTSE 350 provided some details around their cash flow and funding strategies. However this still leaves a large proportion that provided the bare minimum for this critical area.

Explaining the trends and factors likely to impact the future development, performance and position of the business is an area where portfolio companies lead public companies.



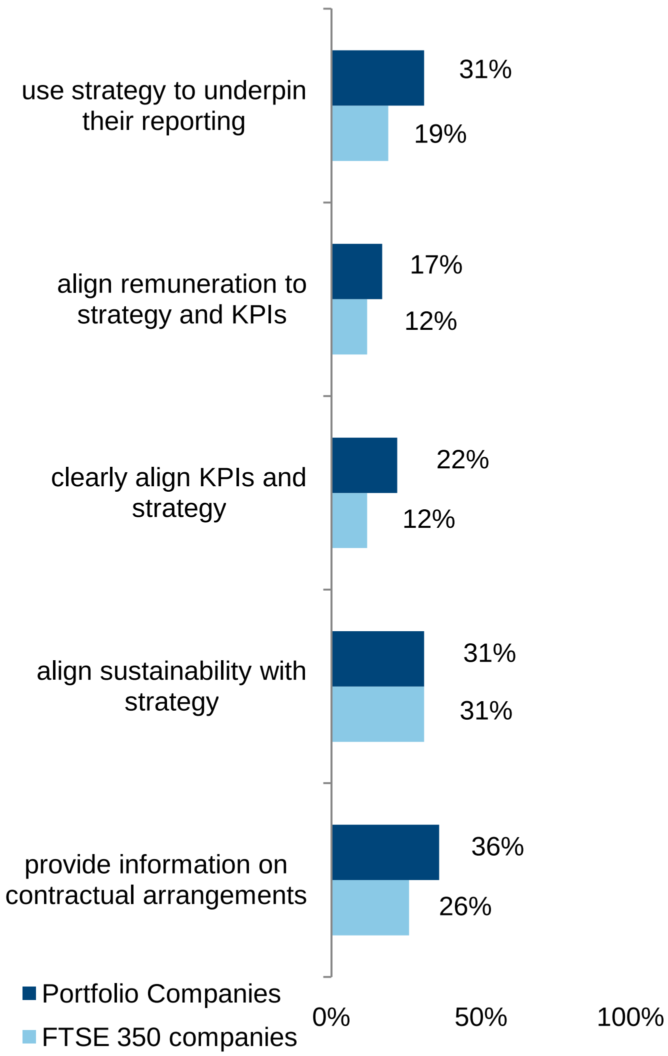
based on reports for years ended between 1 April 2008 to 31 March 2009

The majority of portfolio companies and the FTSE 350 do not use their strategy to underpin their reporting or to clearly align it within their risk assessment and KPIs. However the portfolio companies perform better than the FTSE 350. This would assist in presenting a clear, credible and coherent picture of their performance.

One of the areas of poor performance by both the FTSE 350 companies and the portfolio companies is aligning executive remuneration to strategy and performance against financial and non-financial KPIs.

Portfolio companies and the FTSE 350 provide relatively little disclosure on their material contractual arrangements. Portfolio companies are slightly better than the FTSE 350 in this respect although it is a weak area overall.

On balance the sample of portfolio companies are broadly consistent with the average of the FTSE 350 on the above criteria (ahead in some, behind in others) however it is worthy of note that the areas of better and poorer disclosure are consistent between the two populations.



based on reports for years ended between 1 April 2008 to 31 March 2009

Corporate and narrative reporting requirements of FTSE 350 companies

Corporate and narrative reporting in the UK for FTSE 350 companies primarily include the following areas of reporting:

Financial reporting

At the core of the corporate reporting model is the financial reporting model, consisting GAAP-compliant financial statements and accompanying notes.

Corporate governance

Companies currently need to present a corporate governance statement showing compliance with the 2008 FRC Code on Corporate Governance. This relates to the communication of processes by which companies are directed and controlled. Levels of disclosure differ but would include information on board composition and development, accountability and audit and relations with shareholders.

Executive remuneration

Companies currently need to present a directors' remuneration report showing compliance with the requirements of Companies Act 2006. This relates to the communication of how executives are remunerated, both in the short and longer-term, in order to deliver on their company's strategic objectives.

Corporate responsibility

The enhanced business review requirements under Companies Act 2006 requires companies to include in their directors' report information about environmental matters (including impact of the company's business on the environment), the company's employees, social and community issues and information about policies of the company in relation to these matters, and information about contractual or other arrangements which are essential to the business of the company. The corporate social responsibility report should include communication about how companies are understanding and managing their impact on people, clients, suppliers, society, and the environment.

Narrative reporting

The business review (required by Companies Act 2006) must contain a fair review of the company's business and a description of the principal risks and uncertainties facing the company. The review must include a balanced and comprehensive analysis, using financial and non-financial key performance indicators, of the development, performance and position of the company's business. The business review must also include the main trends and factors likely to affect the future development, performance and position of the company's business.

A FTSE 350 company must also make additional disclosures required by FSA's Listing Rules and the Disclosure and Transparency Rules ("DTR Rules"). The DTR Rules' requirements as to the contents of the 'management report' (ie, the Directors' Report) do not exceed the requirements of the Companies Act 2006 however the directors must also include a responsibility statement in relation to the annual report and financial statements. A FTSE 350 company must send the annual report and financial statements to its members within four months of the end of the financial period to which they relate. In addition to sending out the annual report to members, the directors also have a duty to file a copy with the Registrar of Companies. The DTR Rules also require publication of the annual report within four months of the year end. The Takeovers Directive also brought in additional disclosure requirements on publicly traded companies. The new disclosures include, but are not restricted to, information about company's capital and voting rights, any details of significant interests and any agreements that take effect on change of control of company.

Walker Guidelines for reporting by private equity owned portfolio companies

The relevant reporting requirements for the Walker companies can be considered in three broad areas:

Walker Guidelines specific:

The annual report should identify the private equity funds that own the company and the senior executives or advisers of the private equity firm who have oversight of the company. The annual report should go beyond the Companies Act requirements relating to directors and should give detail on the composition of the board, identifying separately executives of the company, directors who are executives or representatives of the private equity firm and directors brought in from outside to add relevant industry or other experience. The financial review should cover risk management objectives and policies in the light of the principal financial risks and uncertainties facing the company, including those relating to leverage and should include an explanation of the year-end debt and capital structure of the company, its funding requirements with links to appropriate detail in the footnotes to the balance sheet and cash flow section of the financial statements. The annual report should be readily accessible on the company website no more than six months after the company year end.

Business Review (required by Companies Act 2006):

The business review must contain a fair review of the company's business and a description of the principal risks and uncertainties facing the company. The review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include analysis using financial and non-financial key performance indicators.

To comply with these requirements the annual report should include:

- A statement of company strategy setting out what the company is trying to achieve and the priorities for how it plans to achieve those objectives.
- A description of the market in which the company operates as well as how the competitive, regulatory and macro-economic forces impact on the business.
- An explicit identification of the principal risks and uncertainties facing the company.
- An explicit identification of both financial and non-financial KPIs or provide performance data, from which a reader might reasonably identify their KPIs.

The statement of strategy should be clear and prominent and the risks and uncertainties should be aligned with the strategy. Disclosure should include quantification through the use of the KPIs which should be defined and the choice of KPIs explained.

Enhanced Business Review requirements:

The enhanced business review must, to the extent necessary for an understanding of the development, performance or position of the company's business, include:

- a separate clearly headed section setting out the main trends and factors likely to affect the future development, performance and position of the company's business; and

- information about environmental matters (including the impact of the company's business on the environment), the company's employees and social and community issues, including information about any policies of the company in relation to those matters and the effectiveness of those policies; and
- information about contractual or other arrangements which are essential to the business of the company.

Environmental factors should identify those factors which most affect the type of business being reported on supported by quantifiable evidence and targets where applicable. Employee disclosures should go beyond those required by the Companies Act and to the extent employees are a critical resource of the business, there should be a discussion of the management and development of employees including recruitment, training and development and retention practices. Details should be provided at a high level of the social and community issues affecting the business that go beyond details of political and charitable donations. Details of essential contractual arrangements should identify the parties and arrangements involved and not just provide details of supplier payment policies and creditor days.

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