15 October 2007

Mr Andrew Olding
Walker Working Group
3 Clements Inn
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Dear Mr Olding

Disclosure and transparency in private equity

UKSIP welcomes the opportunity to comment on this consultation paper. The society agrees with the finding that reporting arrangements between private equity firms and investors in private equity funds are generally satisfactory. Much of the public criticism of this sector has been driven by political concerns for the public interest rather than by economic issues. The society recognises that transparency can help to serve both investors and the public interest but is concerned that some of the calls for greater transparency are motivated by issues other than the public good.

Detail

The society is pleased to note the distinction made (page 4, paragraph 5) between the two different segments of the private equity market viz. buy-outs and venture capital. Each segment has different characteristics and, as stated, it is only the buy-out market that is attracting criticism. Indeed, many objective commentators hold the view that more venture capital would be beneficial to the UK economy. The private equity industry could perhaps more actively publicise this widely appreciated role of the investment market and so create a more positive image for the industry.

UKSIP would welcome the adoption of the “comply or explain basis” and the “guidelines framework approach” set out in page 4 paragraphs 6 and 7. Such an approach has proved very successful for UK publicly quoted companies. The avoidance of a “one size fits all” compliance approach creates flexibility to allow for unusual circumstances whilst the need to explain can curtail any untoward behaviour or the sweeping away of unpleasant but significant details. UKSIP is, however, concerned how this will work in practice. With listed equity, the “comply or explain” regime allows shareholders who do not accept the explanation provided to engage with the management and board of the company concerned. Ultimately, if such shareholders are not satisfied with the explanation for non-compliance they can either intervene as activist investors or sell their equity holding. Private equity investors do not have either option as the power to intervene rests with the General Partners and, furthermore, such investments are typically long-term and agreements between Limited Partners contain lock-in periods lasting many years. Although such investors, therefore, do not have the power either to be activist or to vote with their feet by selling their shares, their position is generally protected by virtue of the close relationship between the General Partners and the Limited Partners and by the fact that General Partners are usually represented on the

Boards of investee companies. If, however, the increased transparency of the proposed "comply or explain" regime is intended to improve accountability to other parties than investors, it is not at all clear how these parties could exercise any leverage over companies which explain non-compliance in a manner which they deem unsatisfactory

Page 5, paragraph 8: There is a view that there should be a more level playing field with regard to disclosure requirements between private equity companies and non-listed subsidiaries of listed companies and of overseas companies. However, it is not obvious why "larger private companies whose ownership does not involve private equity", for example family owned companies, should be included in these proposals. Such a proposal could create a situation where political concerns specific to private equity result in initiatives that may undermine an important part of the UK's free economy.

Page 7, paragraph 7: Given the political nature of the controversy surrounding private equity, UKSIP is of the view that the thresholds for enhanced reporting should be based on employee numbers rather than any capitalisation metric. It is quite possible for a company with few employees to attract significant capital or for a distressed company with many employees to be acquired for very little outlay.

The society agrees with the items for enhanced reporting mentioned in this paragraph and, in particular, supports the proposal that financial reporting should "cover balance sheet management, including links to the financial statements to describe the level, structure and conditionality of debt."

UKSIP also believes that portfolio companies should report all fees (both the amount and the nature of the fees) paid to the General Partner and to banks. The report on fees should be separate from the breakdown of interest payments.

Page 8 paragraph10, bullet point 5: The society is unclear about the reasons for publicising the Limited Partners in a fund. Unlike shareholders in a listed company, limited partners in private equity have limited rights or powers over the company's affairs. It is not obvious that this is in any way a matter of legitimate public interest. Indeed it could be argued that such publication would be against the public interest as it could lead to a reluctance on the part of some investors to commit funds to private equity and could thus inhibit innovation. It is not clear who would be helped by publication, this presumably being the prime objective of such principles, except that certain stakeholders could try to exercise leverage (see comment above) over investee companies indirectly.

Cont/d…

Pages 13 & 14 paragraph 8: The society disputes the frequently stated but erroneous assertion that "the average holding period of FTSE 100 stocks is substantially less than one year." This is explained in the attached note.

Please contact us if you have any queries.

Yours sincerely

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UKSIP Investment Professional
Advocacy Committee

Will Goodhart
Chief Executive
UKSIP

Enclosure

About UKSIP

The UK Society of Investment Professionals represents the interests of just over 7,000 leading members of the investment industry a proportion of whom are actively involved in the management of private equity. The society, which was founded in 1955, is one of the largest member societies of the CFA Institute and is committed to leading the development of the investment industry through the promotion of the highest ethical standards and through the provision of education, professional development, advocacy, information and career support on behalf of its members. UKSIP supports the CFA, ASIP and IMC designations. Most members hold either the Chartered Financial Analyst (CFA), or Associate of the Society of Investment Professionals (ASIP) designation. The ASIP designation is held by those who successfully completed the Associate examinations. CFA Institute is best known for developing and administering the CFA curriculum and examinations and issuing the CFA charter. CFA Institute's mission is to lead the investment profession globally by setting the highest standards of ethics, education and professional excellence.

Most UKSIP members also belong to the CFA Institute and reaffirm annually their adherence to its Standards of Professional conduct. Both UKSIP and CFA Institute are committed to providing members with a wide range of professional development opportunities. All members are encouraged to undertake ongoing post qualification professional development.

UKSIP is the awarding body for the IMC, the benchmark entry-level qualification for those working in investment management in the UK. The examination is accredited by the Qualifications and Curriculum Authority (QCA) and is designated an 'appropriate examination' by the Financial Services Skills Council (FSSC) for the purposes of the

Financial Services Authority's training and competence requirements. The IMC is held by over 15,000 investment professionals.