



## NEWS

### For Immediate Release

#### **New Study Determines Private Equity Buyout Firms Generally Fail To Deliver Superior Corporate Governance Policies For Companies Taken Public**

***Findings Conflict with Conventional Wisdom that Private Equity Backed Companies Better Align Interests Between Management and Investors***

**NEW YORK, NY, June 10, 2009** – Private equity buyout firms on average do not implement superior corporate governance policies for the companies they take over, restructure, and then take public. Instead, once they go public again, private equity buyout backed companies tend to exhibit features that potentially benefit executives at the expense of shareholders.

A new report released today, *“What Is the Impact of Private Equity Buyout Fund Ownership on IPO Companies’ Corporate Governance?”* finds that companies backed by private equity buyout funds were more likely than others to have classified boards, poison pills, and restrictions on director removal by shareholders. Additionally, the report indicates that lucrative consulting agreements for former executives, generous employment agreements, and special bonuses are significantly more common at private equity buyout backed companies. Finally, the analysis indicates that executive compensation at private equity backed companies tended to be higher, less performance-related, and less at-risk than at comparable companies that did not have private equity sponsorship.

The 90-page report was commissioned by the not-for-profit Investor Responsibility Research Center Institute and conducted by The Corporate Library to examine areas related to private equity backed companies’ ownership, board characteristics, takeover defenses and compensation policies as compared to non-private equity buyout backed companies.

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“Whatever benefits there may be to the private equity model, they seem to disappear once a private equity backed company goes public. The findings are contrary to conventional wisdom and significant for investors,” said Jon Lukomnik, program director of the IRRIC Institute, which commissioned the study.

“The data is in sharp contrast to claims that private equity IPO companies have strong corporate governance structures once in the public markets,” said Paul Hodgson, senior research associate for executive and director compensation, at The Corporate Library. “Instead, private equity buyout firms tend to keep a tight hold on audit and compensation committees, fail to adequately tie executive compensation to performance, engage in many related party transactions with their backers, and structure the companies with stronger than average takeover defenses. The data findings lead to the report’s recommendation that institutional investors with holdings in private equity funds and initial public offerings should encourage private equity funds to improve governance approaches for companies taken public to ensure close alignment of management’s and shareholders’ interests,” Mr. Hodgson added.

In 2007 more than half of initial public offerings had private equity sponsors, and in 2006 they accounted for 22% of deal volume – up from 4% in 2001. While IPO deals have slowed, private equity funds have some \$1 trillion sitting on the sidelines and could be major players again when IPOs increase.

The report’s key findings are as follows:

- **Related Party Transactions** – Companies backed by private equity funds were significantly more likely than the non-private equity backed companies to report consulting agreements with top management, shareholder rights agreements, and registration agreements. Non-private equity backed companies were more likely than the private equity buyout backed companies to have ongoing business contracts and relationships.
- **Takeover Defenses** – IPO companies backed by private equity buyout funds had significantly stronger takeover defenses than companies brought public by non-private equity sponsors. Companies backed by private equity buyout funds were more likely than others to have classified boards, poison pills, and restrictions on director removal by shareholders. Moreover, companies with private equity buyout sponsorship employed certain structural takeover defenses—those that are usually embedded in company charters and thus are most difficult to change—at a higher rate than that seen among the overall US market.

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- **Compensation Policy** – Private equity buyout backed companies displayed poor compensation governance. For instance, the use of tax gross-ups was far more prevalent at these companies. Similarly, lucrative consultancy agreements for former executives, very generous employment agreements, and special bonuses were significantly more common.

Non-private equity backed companies had more simple, straightforward compensation practices pre-IPO that continued post-IPO. Also, non-private equity backed company policies displayed greater diversity in the area of performance metrics indicating potentially more careful efforts to reward executives based on achievements rather than the narrow spectrum of earnings measurement.

- **Compensation Amount** – CEOs of private equity-backed companies tended to have higher total annual compensation than peers at non-private equity backed companies. Only part of the difference can be explained by the size of the companies. Moreover, compensation at private-equity backed companies tended to be less at risk. Finally, CEOs of non-private equity backed companies had more significant shareholdings in their firms than CEOs of companies backed by buyout firms.
- **Ownership** – Immediately after an IPO, private equity buyout backed companies have more concentrated ownership and a higher proportion of shares held by directors and officers as compared non-private equity backed companies. Private equity funds retained a majority of shares in almost half the companies they backed, and they retained significant, although diminishing, stakes in companies for at least a few years post-IPO.
- **Boards of Directors** – For a large number of cases, private equity funds retained control post-IPO over key committees in the companies they brought public by means of directors – including committee chairs – with significant ties to the private equity buyout fund backer. Particularly striking is that immediately post-IPO, a majority of the compensation committee chairs at companies backed by private equity funds had ties to the buyout firm, as did a majority of the directors serving on the compensation committees.

The study is based upon an analysis of 90 companies that went public from 2004-2006, 48 of which were backed by a private equity buyout firm. The sample does not include IPO companies backed by venture capital firms, as this financing typically is working capital rather than compensation to owners of mature companies undergoing a restructure. In addition, the study focuses on governance structures. It does not evaluate operational or stock performance, nor does it offer analyses of overall company performance.

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The full report is available at [www.irrcinstitute.org](http://www.irrcinstitute.org) and [www.thecorporatelibrary.com](http://www.thecorporatelibrary.com). The report also is included in the Social Science Research Network Corporate Governance Network at <http://www.ssrn.com/cgn/index.html>.

### **About The IRRC Institute**

The IRRC Institute is a not-for-profit organization headquartered in New York, N.Y that provides thought leadership at the intersection of corporate responsibility and the informational needs of investors. More information is available at [www.irrcinstitute.org](http://www.irrcinstitute.org).

### **About The Corporate Library**

The Corporate Library is an independent research firm that provides corporate governance information products, research services and data to a broad variety of clients including institutional investors, corporations, D&O liability insurers, law firms, accounting firms, executive search firms, academic institutions and the media. The company produces definitive ratings of U.S. corporate boards of directors, allowing businesses that subscribe to the services to evaluate governance as an element of investment and other risk. More information is available at [www.thecorporatelibrary.com](http://www.thecorporatelibrary.com).

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