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Losing the battles but winning the war: the case of UK Private Equity Industry and mediated scandal of summer 2007

Johnna Montgomerie, Adam Leaver and Adriana Nilsson

CRESC, The University of Manchester

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For further information: Centre for Research on Socio-Cultural Change (CRESC)
Faculty of Social Sciences, The Open University,
Walton Hall, Milton Keynes, MK7 6AA, UK
Tel: +44 (0)1908 654458 Fax: +44 (0)1908 654488

Email: cresc@manchester.ac.uk *or* cresc@open.ac.uk

Web: www.cresc.ac.uk

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Abstract

Private equity was heavily criticised by the media and trade unions during the Spring/Summer 2007, when the Treasury summoned a Selected Committee to quiz its top executives about the business' practices. Despite losing the public argument, the Private Equity industry did not suffer any consequences, escaping with no significant policy changes affecting its modus operandi. Its remarkable lack of sophistication in gathering allies and dealing with politicians and journalists alike diverges from part of the literature on business representation and its assumption that results are directly proportional to lobbying/public relations efforts, be it collectively or individually organised. The argument put forward here is that Private Equity's victory was a consequence of its successful mobilization of existing ideological and structural conditions, leaving to the government the task of justifying any regulatory or tax changes.

Key Words

Private equity, mediated scandal, political representation, Treasury Select Committee, Financial Services

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'THE NEW ROBBER BARONS: City Fat Cats Are Cheating Hard Working Families'. *Daily Mail* headline on private equity, 6th June 2007.

In his 1977 book *The Visible Hand* Alfred Chandler criticised fellow historians for their failure to notice the rise of the modern business enterprise, the arrival of a managerial class and the implication of both to modern capitalism. Instead, he argued, they were more interested in moral judgment on whether business founders were robber barons (exploiters) or statesman (creators), while the financiers were objection of fascination because of the control they seemed to have over crucial sectors of the economy. Some thirty years after Chandler's groundbreaking work about how the separation of ownership and management revolutionised corporate America, private equity – a successful but rather discreet part of the financial sector – was in the spotlight for pressing the rewind button. Using debt to buy ever-larger corporations and de-listing them from the stock market in order to pursue wide ranging restructuring plans, this hybrid type of financiers – in practice both owners and managers – inherited the unflattering title form the British tabloids: the new robber barons.

This article, much like Chandler's work, is not preoccupied with whether private equity partners are or are not robber barons. Our interest here is to understand how, despite open hostility from stakeholders, a full-fledged media scandal and an abysmal performance at a public hearing in front of the Treasury Select Committee, this politically disorganised industry managed to escape virtually unscathed. At the core of our argument is the idea that, as Wyn Grant (2000) remarks on pressure groups in British politics, 'the study of pressure groups is the study of organized interests, although one must always be aware that behind well-defined organizations lurk more amorphous but nevertheless significant bodies of opinion' (p.9). In other words, the success of private equity and its importance as part of the City of London, which in turn derives a great deal its power from the shared assumptions about its crucial role for the British economy, lays at the very heart of the victory, despite the lack of clout of private equity as a interest group. This makes private equity an intriguing case study: it suggests that strategic positioning within a key sector may, in fact, trump even the most sophisticated collective organization, a nuance not adequately considered in the literature.

There are several devices and tactics business or industry groups use to influence policy formation. For instance, by liaising at an industry level business is able to either influence the formation of new policies or prevent changes that could adversely affect existing market practices. Achieving any degree of industry cohesion is no small feat because firms usually interact as competitors and are, therefore, not accustomed to cooperation nor do they have regularized forms of contact (Moran 2006). Especially since the radical changes to business regulatory practice in the 1970s, which weakened the system of interlocking directorships, the British industry as a whole has found it increasingly difficult to achieve any cohesion. These institutional constraints mean firms must typically coalesce around policy events as they arise, in what Moran (2006) calls the 'do-it-yourself' form of political representation.

The limitations business faces in organizing politically are further exacerbated by the tides of digital twenty-four hour media. The potential negative outcomes of media scrutiny or, worse still, a scandal, further challenges business to organize in a way that would prevent large scale public discontent. 'The media's constitutive role in a political scandal is not so much to bring visual evidence of reproachable private acts to the public eye, as to construct the whole scandal narrative in a pre-scripted drama with set roles for the actors involved' (Papadopoulos & Widestedt 2006, p.6). A media-centred scandal attracts political enquiry which could potentially lead to a regulatory response. As a result, business and industry groups must also

now find common ground to address the court of public opinion lest they are drawn into the political arena.

In the spring of 2007, the media facilitated a social panic creating a political scandal for the UK private equity industry. This relatively small and usually reclusive industry did not use any of the usual mechanisms of business representation and successfully navigated a 'mediated scandal'. In fact, the private equity industry arguably lost every battle in the public arena. We evaluate this distinction by analyzing how private equity prevented a regulatory response in the wake of this high profile public scandal. Private equity already benefits from key structural conditions within the UK economy (i.e. the tax and regulation regimes) and the industry effectively traded on existing political commitments to avoid new regulation. This ultimately put the onus on the government to justify any policy changes. Also, the onset of the global credit crunch quickly transformed private equity from marauding corporate raiders needing to be checked, to victims of systemic collapse in need of nurturing from the government and Bank of England.

To evaluate these claims we begin by analysing the contours of business representations in Britain. Next, we consider how key factors contributing to successes of the private equity industry in the post dotcom global economy became the focal points of intense public scrutiny. This public pressure culminated in a full blown media-centred scandal, where a public hearing in front of the Treasury Select Committee exposed the private equity industry to a potential regulatory response. Evaluating both the industry's testimony at the Treasury committee hearing, and the media reaction to it, we demonstrate the degree to which private equity defied common consensus on how an industry 'should' react under such circumstances. Finally, we see in the Treasury's final report on and the Pre-Budget report how the private equity industry escapes virtually unscathed from this maelstrom.

I. The politics of business power

A key aspect of business power is its capacity to mobilize as a collective interest. But as Moran (2006, p.454) rightly points out, the problem facing business is how to articulate this mobilisation, when the market economy presupposes overlapping interests but competitive struggles. In Britain, the coordination of these interests has been historically difficult. Recent developments such as the restructuring of policy making at European level, the rise of a global media and an engaged civil society have revived the importance of collective action.

Two unique features of business power in Britain have hindered the development of a wider system of business representation: the establishment of a system based on private ties between political and economical elites which, in turn, were ideologically supported by the idea of business self-regulation. From the end of the World War II to the beginning of the 70s, a simple word in the Chancellor's ears at a club saying that a particular policy 'was not on' would be enough to stop it from being change/approved (Grant, 1984). Arguably, it was corporations who first experienced the effects of the disbanding of the 'inner circle'[1] of power elites. Mrs Thatcher's open hostility to any form of 'vested interests' embodied in the tripartite system, the government's new ideology of self-regulation and business autonomy inhibited the formation of politically strong industry associations. Corporations were further damaged by a combination of finance deregulation, regulatory reforms and an increasing mistrust and scrutiny from the part of civil society towards large corporations. Under these conditions firms had to find a new way to influence government decisions, and did so with a 'do-it-yourself' approach to political representation (Moran, 2006).

The weakening of the British practice of interlock networks and the social cohesion of the inner circle also affected the City of London. The diffusion of national structures of ownership meant family owned firms central to the old system were slowly replaced by

financial conglomerates, many of them foreign owned and with world-wide operations. The Big Bang in the mid-80s effectively dragged the City' old guard into a new era of liberalized finance, and the 1986 Financial Services Act was the first occasion in which the financial heart of the country started to feel the weight of the new regulatory state over its tradition of self-regulation. The historical event in which the Bank of England lost its position as the City guarantor to the Financial Services Authority (FSA) in 1997, and the Financial Services and Markets Act of 2000, were further blows to the traditional regulatory values of the financial sector. These legislative changes demonstrated to the City the need to explicitly engage in government policy. In a way, it is ironic that during this period where globalizing financial markets and the acceptance of market supremacy acted to legitimise the importance of the City, these same trends pushed it into more formal forms of political representation. Declining social cohesion, internal changes in the roles of trade associations, the Treasury and the Bank of England and the increasing importance of the European Union convinced the City of the importance of establishing trade associations to represent its various financial interests.

The decline of the interlock system and 'inner circle' within the British political system gave rise to new practices of political representation. One track focuses on responding to proposed regulation – lobbying either to amend or to stop them completely – as a way of maintaining or gaining competitive advantage (Harris, 2002). The need to craft appropriate rejoinders that were politically acceptable created a boom in the UK Public Relations industry, especially after the privatisation programme led to a whole new regulatory structure. From 1979 to 1998, the Public Relations industry in the UK expanded by a factor of 32, a 11-fold real terms increase (Miller and Dinan, 2000). Unsurprisingly, the industries most prone to invest in in-house government affairs were the ones subjected to a high amount of regulation and criticism from pressure groups. A survey made with the 100 largest British corporations in terms of total sales revealed that 42% of these companies established government relations divisions from the mid-70s, with firms in the extractive sector (e.g. oil companies) as the most likely to have them (Mitchell, 1990).

Politicians and government officials grew increasingly dependent on lobbying to acquire information for the design of appropriate regulatory responses. Alas, after a first moment of frank distrust – a stage Coen and Willman (1998) call '*ad hoc* approach' – firms realised that 'regulatory relationship could be established with the regulator and that those positions could be negotiated and exchanged for goodwill' (Ibid, p.34). The practices of political representation quickly moved beyond simply responding effectively to the regulators and business began attempting to influence the debate by meeting civil servants, ministers and taking part in technical and expert committees. In other words, business interests had become 'the consummate insiders' (Mitchell, 1997, p.157).

The 1990s, however, would start to show the limits of the do-it-yourself model of business representation. As business and government, both at national and supranational levels, painfully found out, the cosy and not so transparent relationship would be hard to maintain in times of global media and non-governmental organisations, particularly the highly organised and transnational environmental pressure groups. On the financial side, finance report and audit particularly after the 80s and 90s frauds has put the City in an unfavourable light and closer scrutiny, with public agencies moving from the traditionally ornamental bodies to centralised institutions with a proactive approach to the enforcement of rules, following a hardening of the regulatory framework. Even though the efficiency of the DIY method was not an issue, the reputation and image of firms using it and of governments altering or haltering policy because of it was definitely in check.

Part of the problem started at European level, with the overloading of the European Commission with individual business lobbying. To overcome the 'legitimacy deficit' accusation hanging above its head, the European Commission started to restrict access to its forums. The changes forced firms to diversify their lobbying strategies by including collective

bodies of representation and consensus building in their syllabus in order to establish a legitimate status in policy making. Successful European lobbying, from the 90s onwards, had less to do with monitoring and defensive action and more with having organisational capacity to form political alliances and to create or reinforce collective representation via traditional political channels, which meant a need to coordinate a multilevel lobbying strategy involving national and supranational actors. The firm's ability to influence policy has been definitely linked to a positive image as a provider of reliable encompassing information, weakening the do-it-yourself approach.

A quick look at the recent literature analysing business representation shows a strong focus on the relative success or failure of mechanisms for extracting policy concessions (Leblond, 2008 , Verdun, 2008 , Smith, 2008). Here, different factions within the financial services industry act as economic interest groups which seek to influence those policies most relevant to them. At the industry side, a crucial part of the current strategy is directed to the traditional forms of collective representation, namely the revitalisation of the European federations – and, to a lower extent, the national associations as well – and the building of coalitions of interest geared toward common objective in particular issues (Coen, 1997). Establishing a 'European identity through pan-European alliances with rival firms and/or solidaristic links with societal interests' has also become crucial (Coen, 1998, p.78). The general consensus appears to be that in order for any business sector to be successful in the political arena, it must mobilize resources into strategies of public engagement and rebuttal.

In sum, the general belief is that successful business representation in the political arena – for both industry and financial services – entails the ability to form a collective interest, for example by establishing an industry body. Banding together in the face of policy change at the industry level, and if possible through broader sector-based coalitions, is seen as a necessity if business interests are to be incorporated into policy. In this way, economic interest groups, it is argued, can effectively influence the policy process. Moreover, in the age of twenty-four hour media coverage the importance of public relations savvy can mean the difference between proverbial life or death for an individual business or industry. In the light of these changes, large amounts of resources are dedicated to public relations, brand management and public affairs divisions to deal effectively with the public and government.

The UK private equity industry case to be analysed in the next section, however, challenges many of the key assumptions put forward by the current literature. The UK private equity industry does not have a well-organized, or competent, trade association. The British Venture Capital Association's (BVCA) only event is a yearly dinner and they made only one proscriptive attempt to extract policy consensus. Deep divisions within the industry between three different factions (venture capital, mid-cap funds and the large buy-our funds) obstruct the possibility of forming, let alone mobilizing, a collective interest. The uniqueness of this case study is not the private equity industry's ability to extract policy concessions from the UK government. On the contrary, what makes the Private Equity industry so interesting is that it was able to exist virtually unencumbered by government interference despite its high profile behaviour.

II. Private Equity in the UK: The Conditions of Growth and the Enrichment of General Partners

If we are to try to understand the process of policy change through the lens of political organisation and lobbying, we need first to understand a bit more about the activity of private equity before exploring the regulatory and tax environment which underpinned the growth of the private equity industry throughout the 2000s, and which the industry fought to protect.

After the dotcom bubble burst in Spring 2000, the private equity industry, in particular large-cap funds, concentrated mainly on buyouts rather than start-ups. Private equity companies applied a simple formula for generating returns, which involved drawing both debt and equity into managed funds in order to buyout, or take minority stakes in, public or private firms companies. Generally, the conventional capital split of the buyout fund was 30% equity to 70% debt (FSA 2006), with the debt generally loaded onto the purchased company's balance sheet, and often paid down gradually from operating cashflow. Whereas banks would normally supply the 70% debt, private equity General Partners (GPs) who manage the fund and oversee the company would supply 2% of the total equity with the remaining 98% of the equity supplied by passive investors, mostly institutional investors who are known as the Limited Partners (LPs). The normal aim of a PE buyout would be to dispose of the purchased company within a timeframe of 3 to 5 years by trade sale or flotation; and the fund as a whole would be wound up within 7 to 10 years, after which point the profits of the fund would be distributed (Froud and Williams, 2007).

However, under private equity the profits of the fund are unevenly distributed, with GP's taking a far greater share relative to their original 2% equity input. Rewards to the GP take two forms. First GPs claim a management fee of around 1.5-2.5% of the total funds managed (Walker, 2007, p.12). This is non-performance related and claimed by the GPs whether the funds create or destroy value in the firms they manage. Additionally, GPs receive 20% of the profit or 'carry' from the sale of the companies managed by the fund, where the size of the profit depends on multiple conditions like the state of the new issues market or the availability of trade buyers at point of sale.

Such propitious 'terms of trade' are coupled with significant regulatory and tax benefits, which the private equity industry has material interests in preserving. First and foremost, the private equity industry benefits from limited liability status, which confers certain regulatory and tax benefits to the activity. As limited companies, private equity funds are not regulated under the same framework as other financial intermediaries like pension funds, who also invest other peoples' money in trust. Furthermore, the companies bought out by private equity funds assume limited liability status, which means they are not required to report on their business activities or financial performance as other public companies must, and also means the fund is not liable for the bought-out firm's debt obligations should it file for bankruptcy. Limited liability status thus provides privacy for the activity of private equity managers which gives greater latitude for asset sales, debt issue and other kinds of financial engineering than in a publicly listed company, but also means they can sidestep the risks associated with such moves when the firm, not the fund, is liable for any outstanding claims if the firm becomes insolvent.

Private equity funds also benefited from a particularly favourable tax system, which enabled them to take a larger share of the profits made on their investments. Principally, private equity is a trading business that buys and sells used companies. Notionally the industry includes venture capital funds (i.e. start-up funds), mid-cap funds (i.e. those managing less than €100 million) and large-cap funds, but practically large-cap funds have historically been most important in value terms, accounting for 70% of private equity activity in 2006 (IFSL, 2006, p.8). Yet, even though trading is the primary activity of the private equity business, the profits realised on investments (called 'carried interest', or just simply the 'carry') are taxed as capital gains rather than income, unlike most other profit sharing schemes in the financial services sector. Such benefits are multiplied if the private equity fund holds a company for longer than 2 years, because under the taper relief system, the capital gains tax rate is reduced to 10%.

Similarly, the UK tax system offers relief for interest payments on debt. Large amounts of debt are applied to the equity stake to buyout other public or private companies. However, this debt is treated as a business expense and so interest payments on that debt are tax deductible,

leaving more cash in the bought-out firm for investment or dividend payouts. Finally, lax regulatory conditions and an abundance of tax loopholes meant that the claims on the proceeds of large-cap funds were structured in increasingly complex ways. The funds in their own right are mainly structured as limited partnerships, or some other tax exempt vehicle, often legally based in offshore tax havens. Besides, the use of non-domicile status and the payment of gains into a complex structure of holding companies meant private equity fund partners often took an even greater share of income at the expense of the Treasury, and made profits increasingly difficult to trace.

All of this was relatively inconsequential while private equity remained a small part of the financial sector, and buyout funds invested mainly in small and medium sized enterprises. But throughout the 2000s, a series of conjunctural developments facilitated the growth of the UK private equity industry, which is now the second largest in the world next only to the US in terms of size of funds raised and assets under management (FSA 2006). Throughout the 1990s, private equity funds took advantage of low interest rates, high levels of liquidity and absent covenants on loans to borrow cheaply from the banks and scale up their acquisitions, particularly in the UK (Folkman et al., 2007, Froud and Williams, 2007, Wharton, 2006). This trend was further facilitated by the changing investment preferences of pension and mutual funds who sought new ways of improving returns given the post-dotcom bear market in publicly listed stocks, just as financial actors began to see opportunities in PE due to the favourable taxation system.

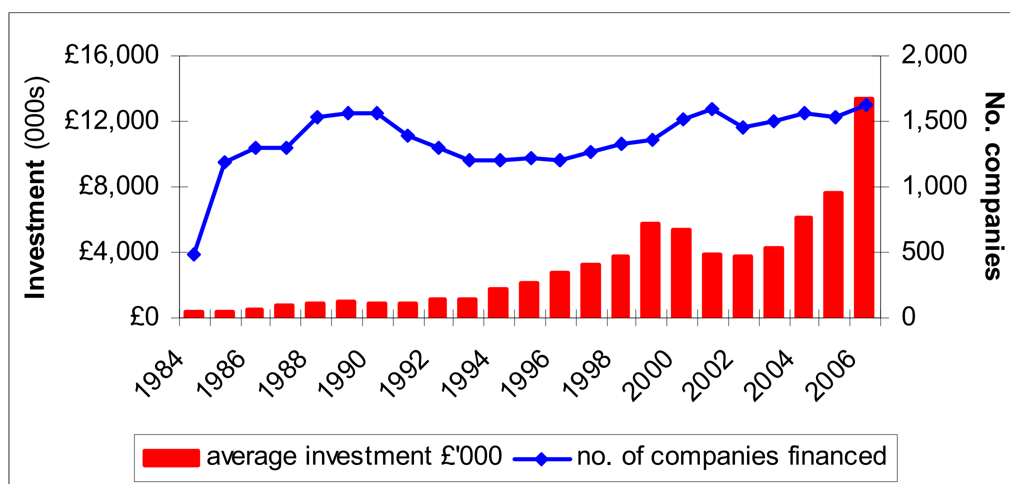

Figure 1

These conditions combined to produce a spectacular growth of large or mega buy-out funds that attracted unprecedented levels of investment. As figure 1 shows, private equity buyouts experienced hockey stick-like growth; while the number of transactions remains relatively constant, the size of deals grew precipitously throughout the mid-2000s. Total deal value of UK private equity deals rose fourfold, from $16.3bn in 2001 to $68.4bn in 2006 (Thornton, 2007, p.11). This trend reflects the general dominance of London in world financial markets, which provided opportunities for US practitioners and practices to escape the constraints of Sarbanes Oxley and flourish in a ‘lighter-touch’ British setting (Folkman et al., 2007). Moreover, 80% of PE equity funds come from US institutional investors, particularly pension funds, rather than from UK or European sources.

Yet, the increasingly high profile buyouts of household names such as Boots, the AA, and the attempted buyout of Sainsbury’s, intensified publicity and criticism from Trade Unions and the media. And it is to this question that we now turn.

III. Culmination of a mediated scandal

The high profile purchases of large high street brands took private equity from the inner pages of the financial press to the front pages of the mainstream broadsheets and mid-range tabloids. The growth in size and visibility of private equity brought with it Trade Union and media revelations about GP's exorbitant pay and their seemingly unwillingness to pay enough income tax, the draconian management style and neglect of workers rights in their acquired firms, and the destabilising effects of debt-funded acquisition on the economy more broadly. The adverse public response is perhaps unsurprising, given well-documented growing distrust of Big Business in a range of surveys (Lewis, 2003) and academic papers (e.g. Moran 2006); the case of private equity, nevertheless, is unusual because the industry's response to the campaign was so poorly coordinated and weak. It would be easy to presume that, as powerful and wealthy actors, the private equity industry could mobilise physical and financial resources quickly to counter such negative representations of their industry. Instead, the private equity industry proved itself deeply divided and its industry body appeared to lack the necessary skills for media manipulation and public engagement. The result was a fully blown 'mediated scandal' which exposed the private equity industry to a potential regulatory response.

Successful engagement with the media is increasingly important to business, especially to control the outbreak of public scandals that more often than not result in legislative change. Scandals are produced when relatively discrete phenomena are exposed and media representations discursively constitute or frame the moral outrage around the purported transgression. The media's constitutive role in a political scandal is not so much to bring visual evidence of reproachable private acts to the public eye, as to construct the whole scandal narrative in a pre-scripted drama with set roles for the actors involved (Papadopoulos & Widestedt 2006, p.6). Typically, media scandals depend on revelations and claims that are followed up by further disclosures and/or counter-claims, which often build to a climax and occasion some form of socially or morally approved sanction (Lull and Hinerman, 1997)

Scandals are thus 'made' and the production of a 'mediated scandal' is a process that runs through a series of stages. This normally begins with the identification of a transgressive act(s), which are then disseminated through mediated forms of communication like newspapers, television etc. (Thompson, 2000, p.66). This stimulates a series of claims and counter-claims between two parties, played out across the national press making information open-ended and self-referring as newsflow escapes the original temporal and spatial context. The media plays a key role in framing/shaping the contours of the discussion, often drawing on its own and others reports to add weight to the scandal. Finally, once this becomes a fully blown scandal, there is often a culmination in the form of a trial or public hearing, during which there is iterated reflection on the relative merits and demerits of the hearing's results.

The media coverage surrounding private equity in the run up to the Treasury Select Committee (TSC) is reasonably faithful to this process of 'mediated scandal'. The basic contours of the scandal can be traced through frequency counts of private equity articles in a sample of broadsheet and mid-market tabloids between January 2001 and June 2008. The graph demonstrates only modest and unstable growth from 2001 to around the end of 2004, as a growing number of newspapers covered the ebb and flow of individual private equity takeovers. However, after 2005, we see more significant rises in press coverage, with a significant spike for 6 months in the middle of 2007, reflecting the announcement of the TSC in March 2007 for June of that year. This period also reflects the peak of Trade Union campaigns, media scandal stories and unfortunate practitioner gaffs, as the announcement of the TSC became a catalyst for further negative media reporting in its own right.

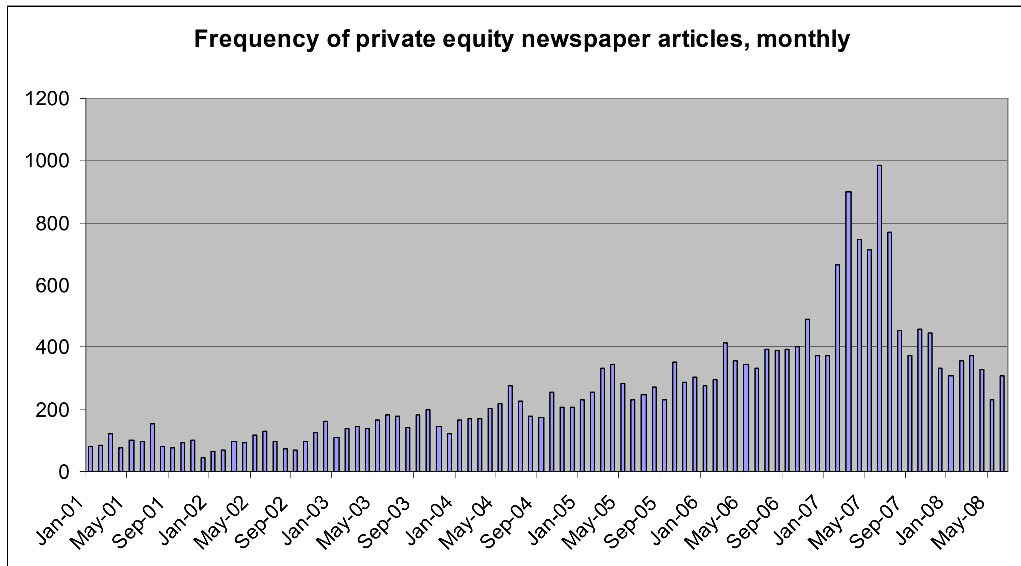

Figure 2

Yet frequency counts of private equity stories only tell us so much, and so it is necessary to add substance and texture by emphasising the tone and character of these reports, and how criticisms of the industry intensify in the lead up to the TSC public hearing. Private equity's self-representation could be subdivided into two phases. The first, prior to the scandal, when the industry lacked a coherent and clear 'narrative' about its activity, the second as private equity representatives hurriedly constructed a defensive narrative to protect the legitimacy of the activity by countering directly the various claims about asset stripping, tax avoidance and general avarice.

The scandal originated in a campaign by the GMB (Britain's General Union) in response to private equity firms CVC Partners and Permira's takeover of the Automobile Association (AA) in 2004. The lack of disclosure by the private equity GPs when the GMB attempted to discuss their plans for the AA unnecessarily provoked a key stakeholder. The GMB were told in no uncertain terms that 'private meant private' and that neither fund was under obligation to discuss their management strategy with the Union's membership. Attempts to draw the GPs out into consultation involved sensational direct action protests. The GMB used the biblical metaphor of 'the chances of rich man getting into heaven' by staging a large camel and a small needle outside of Permira managing partner Damon Buffini's church. Also, AA/Saga boss Andrew Goodsell had a makeshift 'chicken farm' constructed in his village after he reneged on a deal previously struck with Mr. Buffini that would see the GMB re-recognised in the workplace. The GMB's media savvy attracted national press attention. These campaigns were enormously effective, gaining important column inches and television coverage through organised and persistent campaign work, successfully embedding the association between private equity and 'asset stripping'. But the private equity partners continued to cling to some notion that they could had a right to operate without any outside influence.

The GMB sustained its campaign against private equity by publicizing the various measures adopted in CVC/Permiera post-takeover programme. The shedding of 3,400, or one third, of the AA's workforce (Times 12th April 2006), gained momentum as further stories of computerised timing of toilet breaks (Guardian 31st October 2005), notifications of redundancy by text message (Times 6th February 2006), forced overtime (Guardian 14th February 2007), and bullying and harassment by managers (Times March 26th 2007) began to work their way into the national press. These worsening conditions for ordinary workers were

juxtaposed against the enrichment of the private equity partners overseeing the firm. Also, consternation arose following the decision by the General Partners to extend the level of debt loaded onto the AA's balance sheet from £1.3bn to £1.85bn in order to realise a £500m 'special dividend' bonus payout (Sunday Express 26th February 2006).

For Thompson (2000), individual scandals such as the one at the AA have the potential to overflow into new areas, as information flows spill out and, in turn, as new examples are discovered which confirm the previous objections. In this case, the GMBs campaign received the backing of sympathetic MPs like Gwyn Prosser, and broad support across the unions who voiced their position against Permira and the AA. Similarly, at a European level, Phillip Jennings, general secretary of the UNI global union, announced that private equity had been operating 'very much in the dark' and that Trade Unionists should 'bring them out of the shadows' (Guardian 26th Jan 2007). The result was a focused effort drawing on sympathetic actors inside and outside the labour movement who lobbied for industry-wide reform, including the abolition of taper relief and, in the case of the AA, the removal of its limited liability status (Guardian February 11th 2007). The experience of the AA acted as cautionary tale for other private equity takeovers, and stimulated mobilisation against, for example, the threatened private equity takeover of Sainsbury's (Guardian February 11th 2007) and the potential £800 million sale of National Car Parks (NCP) to 3i. Public and media attention reached a fevered pitch with the announcement of the £1bn buyout of Alliance Boots by AB Acquisitions (a consortium of KKR and Stefano Pessina) in June 2007.

Criticism was not confined to the world of organised labour however. Renowned investors like Warren Buffet criticised the '2 and 20' fee structures of the 'helpers' in private equity and hedge funds because they ratchet up the charges for owners (i.e. pension funds); while famed hedge funder Barton Biggs (2008) questioned private equity's claim to be able to generate returns over and above the public markets. Chairman of SVG Nicholas Ferguson's admission that private equity partners paid 'less tax than a cleaning lady' sparked most outrage in the media. In the week that followed the 5th June 2007, the quote was reported across broadsheets like the *Guardian*, the *Times* and the *Financial Times* as well as the mid-market tabloid press like the *Daily Mail* and *Express*. The media fallout soon spilled over into the BBC and economic periodicals like *The Economist*, *Moneyweek* and *Business Week*, giving the offending quote an international stage. The quote was used to exemplify the emergence of 'Wild West Capitalism' where private equity 'corsairs' strip company assets, close company pension funds and take advantage of tax loopholes for personal gain (Guardian 5/6/07). Others like *The Times* highlighted the inequity of a tax regime brought to light by Ferguson's comments would 'enrage Middle England' (Times 5/6/07). In terms of the mid-range tabloids, the *Daily Mail* in particular ran a series of articles, depicting private equity practitioners as 'City Fat Cats' and 'locusts' (Daily Mail 5/6/07), 'new robber barons' (Daily Mail 6/6/07) and later, 'pillagers' (10/6/07). The *Mirror* meanwhile pondered if the large paypackets and low tax rates meant we had effectively returned to feudal times (Mirror 7/6/07). Only really the *Telegraph* defended the industry, highlighting its innate efficiency and its general benefits to the UK economy.

Trade Union campaigns, City scepticism, and practitioner gaffs mediated by the national press helped to construct a social panic around private equity and illustrates Thompson's observation that scandals are continuously, 'refined and revised as the events unfold'. It also highlights the often contingent and unpredictable turn of events, and thus their organised and disorganised elements, mediated through a national media that frames the subject, feeding on its own output in the production of news and vilification of certain actors/groups. In short, the timing of Ferguson's comments ensured that the discussions in and around the Treasury Select Committee would be at the very forefront of media focus. However, as Thompson notes, scandals are a process of claim and counter-claim and so it is important now to turn to the response of the private equity industry.

IV. Private Equity and Public Defeat

It is unanimously agreed that the private equity industry body, the BVCA, and the large-cap funds gave a feeble performance in their oral evidence to the Treasury Select committee. Poor public engagement fuelled the on-going media frenzy over the excess of the private equity industry. Combative and ineffectual testimony in front of the committee by the BVCA and General Partner's of large-cap funds led to open animosity in the public hearing. At the second session, MP George Mudie (Labour) warned the large-cap fund GPs to take the proceedings seriously: 'Your predecessors [the BVCA] got savaged because they treated us like mugs and would not answer straightforward questions' (20 June 2007 Q287 p.39). The BVCA performance as universally panned by MPs in the press as 'bland' and 'obstructive' with the BVCA accused of 'behaving like ostriches' (Financial Times 14/7/07). The weak performance of the industry bodies also became the topic of much press coverage over the following week, with the FT describing the submission as 'defensive and complacent' (13/6/07), the Guardian (19/6/07) claimed the BVCA was 'slaughtered' by the committee, and the Observer (17/6/07) concluding that the weak performance signified that, 'private equity's unfettered, unscrutinised bonanza is over'. Indeed the criticism of the BVCA were so vehement that chairman Peter Linthwaite was forced to step down from his position, just one day after his submission (FT 14/6/07).

In the intervening week between the BVCA testimony and the appearance of the large buy-out GPs in front of the committee, pressure mounted to realize a positive public performance. Permira reportedly paid £1 million for advice from Peter Bingle, chairmen of renowned public affairs consultancy Bell Pottinger who specialize in navigating business through major reputational crises such as McDonald's at the onset of the BSE crisis and the Police Federation through the Sheehy inquiry.

The TSC oral evidence revealed the stark divisions with the industry between the large-cap funds and the mid-cap funds. These two groups presented evidence on separate days and gave very different accounts of their practices, exposing the high degree of fragmentation within the industry. Drawing on claims of current literature on business representation suggests the failure of the Private Equity industry in the media and at the Treasury Select Committee hearing stem from the inability to mobilize a collective industry voice. The level of industry discord was so obvious to the committee that Chairmen John McFall (Labour, West Dunbartonshire) pointed out with dismay: 'But there is not a unified voice coming from private equity, is there?... look at the scale of the fighting in the past week. Get real! What I am asking you is: can you get your act together?' (TSC, 20 June 2007, Q238/240 p.34).

The written and oral evidence exposed the marked differences between the large buy-out and the mid-cap funds. It became clear that the large-cap funds are not only bigger in size and scope, but operate in separate arena from the mid-cap funds. Notably the substantial American contingent amongst the large-cap funds, compared to exclusively British representation in the mid-cap funds. American mega-funds like KKR, Carlyle and Blackstone have an advantage via their existing relationships with large US pension funds, which are the largest investor in big UK buy-out funds. In some instances, the factions within the industry led to instances of 'friendly fire' where testimony by mid-cap managers caused some damage to the large-cap funds. For instance, mid-cap fund Alchemy's John Moulton explained how large-buy out funds are able to use their scale to extract higher management fees, raise bigger funds and make ever-larger purchases. 'A proportionality of our industry, we are takers of a market that is giving it to us. The institutions give us the same terms essentially for a £100 million fund as for a £10 billion, 100 times the fees and income. The costs of running the funds do not go up by a factor of 100' (TSC, p.76). The BVCA attempted to gloss over this fragmentation by cultivating the common lineage of the UK's private equity as an outgrowth of the venture capital industry, although no venture capital firms were represented at the inquiry.

Poor public engagement besieged the private equity industry by fuelling distrust of their business practices and questioning their overall legitimacy as a major actor in the UK economy. During the course of the mediated scandal private equity funds were repeatedly accused of being ruthless asset-strippers which practice 'casino capitalism, to make huge amounts of money for General Partners and their investors, while ruining the lives of the ordinary worker. Their business practices were depicted as value extraction as sophisticated financial engineering techniques transformed established firm at the expense of the work force and future growth. The industry addressed this attack on their legitimacy by using a buckshot approach. This involved naming the multiple benefits of private equity investments rather than putting forward a collective view. This included referencing individual practitioner's investment record, claiming private equity solved existing management problems within firms also that private equity benefited the entire UK economy by creating profits for pension funds and jobs for the workforce. In effect, the private equity industry was all things to all people.

The micro-level story put forward by the BVCA emphasized private equity's economically efficient governance arrangements, in particular the industry's ability to resolve agency problems through greater surveillance of management. 'Private equity makes managers into owners, giving them the freedom, focus and finance to enable them to revitalise their companies and take them onto their next phase of growth'(BVCA, 2007b, p.3). This claim was sought to explain that the innate efficiency of the private equity model, rooted in the governance arrangements of the firm, as providing material benefits for society more broadly. Various publications and interviews highlighted the many apparent beneficiaries of private equity, ranging from investors to the Treasury to the workforce. The industry argued that the superior returns of private equity means that pension fund investors, and therefore pensioners themselves, stand to gain from its growth (BVCA, 2007c, p.1). Essentially the industry body tried to claim that private equity could be all things to workers, investors, and the firms they acquire. Not only does private equity make a dynamic contribution to the economy, it can bring a new sense of direction to long-established businesses. Moreover, successful acquisitions could lead to new investment and more jobs. When a firm is re-listed on the public market after a period of private equity management, they often create above average returns for their new shareholders. Perhaps it is no surprise that such fantastic claims where greeted with intense scepticism.

The arguments that the activity of private equity were short-termist and involved 'asset stripping' were more critically engaged, arguing that private equity time horizons are longer term than in public equity. Furthermore, the industry body argued that because private equity is a trading business, practitioners can only make money when the companies are viable: 'we make money from building and growing the companies we own. We make money from creating value', as Kolade argued in interview to Sunday Express. The accusation that private equity firms were downsizers was universally denied. Special focus was made of companies like Fat Face, where employment had apparently grown by an average of 47% per annum under private equity ownership (BVCA, 2006). The criticisms about tax were sidestepped by simply listing large nominal sums paid to the Treasury, for example: 'public revenues receive significant contributions from private equity-backed firms…During the last tax year, they collectively contributed £4.3 billion in corporation tax, £8.7 billion in PAYE & NIC, £12.1 billion in VAT and a further £1.3 billion in excise' (BVCA, 2007a). The emphasis on mutual or collective gain was not so much an attempt to claim the industry was motivated by altruism, but instead was used to 'paint out' discussion of partner enrichment by illustrating universal gains. There was no real attempt to even discuss rewards as 'just deserve'. Indeed deflection rather than direct engagement was a key tactical device used by the industry to sidestep rather than engage with public criticisms.

Efforts to put forward the multiple benefits of private equity and the universal gains realized by their business activities were ultimately unconvincing because of the lack of corroborating

evidence. Since private equity funds do not publish annual reports, as PLC must do, there is no data to evaluate the claims of value or job creation. The testimony of academic expert Prof. Karel Williams repeatedly pointed out that the evidence on private equity's performance were by no means clear: 'Private equity portrays itself with a justificatory narrative but the evidence on job creation and superior returns is mixed and ambiguous' (p.112) The data provided by the BVCA was highly stylised using selective vignettes of individual companies improved by private equity management. The widely quoted factoid that the private equity-backed firms employ 19% of the private sector workforce in the UK prompted an independent submission to the Committee from renowned financial services expert Dr. Tony Golding, who took serious issue with the methodology used and conclusions reached by the BVCA study: 'This figure is highly misleading….the 19% refers to every company that HAS EVER received private equity funding, including those where private equity is no longer involved because it has exited' (p.182). Without reputable evidence to substantiate their claims the private equity industry's effort to legitimize its business practices and stem the tide of negative media attention were seriously undermined.

Alongside the weakness in the evidence the industry suffered from its inability to provide a cohesive and plausible account of its business practices. In particular, the large-cap funds suffered from the obvious fragmentation within the private equity industry between its practices and those of venture capital and mid-cap funds. During the committee hearing MP Angela Eagle explicitly warned the BVCA's Mr. Kolade: 'Do not hide behind venture capital' (Q117, p.18) after industry representatives repeatedly obfuscated the unique practices of large-cap funds. Moreover, the testimony of General Partners of mid-cap funds often distanced themselves from their larger brethren. In addition, the large-cap funds made another strategic error by choosing to describe the strengths of their business practices relative to weakness of other major actors within the financial services sector, in particular Hedge Funds and Institutional Investors. Conventional wisdom on the power of business representation suggests that creating alliances, or common objectives, at sector level provides even more political clout than basic industry cohesion. The large-cap funds took the opposite track by claiming they create value because of distortions brought about by the long-term dominance of institutional investors in financial markets.

> More concretely, PE/VC firms also distinguish themselves from short-term [institutional] investors by the way they manage their investments. Short-term investors take advantage of market trends but do not influence the way the underlying companies operate. In particular, PE Buyout firms have an opposite strategy, which first aims to improve the health of underlying companies in order to fully benefit from favourable market developments. (EVCA written submission: p.126)

This is a very peculiar strategy to deploy since institutional investors are the single largest contributors to private equity funds. Moreover, the large-cap funds went to great lengths to trade on their long-term investment strategies as infinitely better than the short-term strategies of hedge funds, essentially opening a two front public relations war with other segments within the financial services industry. Admittedly, in the case of hedge funds, the large buy-out firms took their cue from the Financial Services Authority (FSA) report on private equity which used hedge funds, a group they have been at pains to come to grips with in their regulatory framework, as a comparison group (See Financial Services Authority, 2006). The fall-out from this tactic became apparent as leading hedge funds took to the media to point out the failings of the private equity industry. These points were then brought up in the Treasury committee hearing: 'Jim Chanos, the founder and president of Kynikos Associates, the world's largest dedicated short-selling hedge fund. He says that he has a problem with private equity in that it depends upon an amazing discontinuity and arrogance which is that the stock market is totally underpriced at all times and it is unbelievable to think that the market is stupid at all times' (30/06/07: p.33). These actions attracted criticism from sections within

financial services that would have otherwise been wholly supportive of preventing a regulatory intervention by government solely on ideological grounds.

V. Private Equity's Victory

By all accounts, the large-cap funds and the private equity industry body, the BVCA, gave an abysmal performance in the media and at the Treasury Select Committee. Failing to secure any collective vision or argument on behalf of the industry, providing no independent evidence to back up their claims to social legitimacy and unnecessarily antagonizing potential allies in the financial services sector should have resulted in a resounding defeat for the industry. On the contrary, the private equity industry and the large buy-out firms came out of this experience relatively unscathed by any systematic or targeted regulatory response. Instead, they were left to implement their own 'insider solutions', namely to adopt the voluntary codes outlined in the Walker Commission, and to some additional monitoring by the FSA (see: Treasury Committee, 2007b, Walker, 2007).

The ultimate success of the private equity industry came as a result of its successful challenge to the government to adhere to its own political commitment to a clear and fair tax system. Also, the industry repeatedly pointed to the existing regulatory framework suggesting it was these bodies that were responsible for setting the criteria of regulation. Finally, private equity was able to prevent a regulatory response by the government by asserting that its business practices were operating within the law and that any changes to tax or regulation would ultimately affect all of UK business. Essentially, this meant that the government would have to either justify singling out the private equity industry as an exception to the rules, or risk harming other businesses.

These tactics challenged the government to be politically coherent in the policies it applies to business practice. The private equity industry counter-attacked by pointing out that any attempt to change tax rules would also affect all business in the economy. Moreover, any targeted intervention to exclude private equity from taper or tax-deductions on debt would be to single out an industry for growing too quickly or being too profitable. This would run counter to New Labour's political commitments of simplifying the tax code and could put its own legitimacy with the business community in question. By framing the debate in this way, the private equity industry geared the debate toward questioning the government's practices rather than their own. They successfully side-stepped the issue of how private equity uses current tax rules to extract huge profits that are not adequately taxed and re-distributed through society.

This left the politicians in the TSC to argue on the grounds that the tax rules were not being used as intended (TSC, p.46). To some degree this is true, as both taper relief and tax deductions on debt were implemented with the intent of rewarding investments in long-term organic growth by promoting enterprise and the venture capital industry. The use of these tax concessions by an investment fund does raise important concerns but, again, this applies more to the case of the large buy-out rather than mid-cap funds. Given that large-cap funds are primarily engaged in buying well established public companies, already engaged in long-term investment in the economy, it is not exactly clear whether they qualify for tax concessions for debt acquired in taking company private and tax relief on profits realized in re-listing the company on public markets. Many sceptics pointed out taper relief and tax concessions on debt gave private equity unfair advantages, creating distortions the tax treatment of company revenue and the wider market.

Crafting a political engagement strategy based on challenging the government to keep its political commitments is compelling because it speaks directly to notions of equal and fair treatment for all business. Moreover, the large buy-out firms strategically focused on the

preserving the current tax structure by claiming the industry enjoyed no special treatment and was doing nothing illegal. The consistent response of private equity witnesses was to continuously point out that the tax regime for private equity is the same as for other UK companies and individuals. 'Despite press and political claims to the contrary, the private equity industry enjoys no tax advantages over the rest of the economy' (TSC, p.152). Similarly, the BVCA continually repeated the same position with relations to private equity and taxation, 'We do not make the tax rules' (p.16) a point echoed by industry practitioners 'Debt is tax-deductible for every single company in the country—full stop' (p. 47). Strategically highlighting that the regulatory and tax regime were outside the private equity industry's influence, and that these were rules applied to all businesses equally, benefited the large-cap funds. By framing the political debate in this way, the private equity industry essentially gave the government an ultimatum: change tax code, which will affect all business, or find a legitimate reason to single out this industry. In doing so, put the onus on the government to justify its actions. This made keeping the status quo the simplest options, the most desirable outcome for the private equity industry because it could continue its business practices unencumbered by new tax rules.

Moreover, the private equity industry deferred many of the questions regarding the adequacy of current regulation to the various bodies in charged with oversight and intervention. Every written submission provided by private equity addressed the question on excessive leverage by deferring to the European Central Bank's one and only report on private equity (European Central Bank, 2007). A similar approach was adopted dealing with the question of potential systemic risk arising from excessive leverage as every private equity submission deferred to the Financial Services Authority (2006) one discussion paper on private equity. Again, there was no systematic engagement with the data offered in the discussion paper, instead it was invoke as an authoritative conclusion that systemic risk was a remote possibility. Finally, throughout the written and oral evidence, private equity deferred to the uncompleted and unpublished Walker Consultation (2007) on Transparency in Private Equity as the adequate route for industry change. This tactic offered the government an 'insider solution' to the problems associated with non-disclosure on conflict of interest highlighted in the committee hearing. Sir David Walker's career makes him a well connected industry insider.[2] Walker's report offered new voluntary codes to address disclosure in the industry and made non-binding recommendations for better communication with stakeholders. This light touch options was crafted as an acceptable compromise by the industry, when in fact it was clearly much better than a regulatory requirement for disclosure and stakeholder negotiations.

Industry witnesses used this tactic to defer to other actors as responsible for outcomes of private equity investments. For instance, the private equity managers took every opportunity to claim that their investments benefited pension funds, but when asked what steps the industry took to protect pensions, the BVCA representative simply deferred to the pension regulator:

> Private equity operates under the same rules and the same pensions regime as any other public company and there is a pensions regulator in place that we would seek to go and talk to when we are taking over a company which has a pension fund which may or may not be in deficit, that we want to get involved with […] there is no special thing about private equity, we operate under the same regime as everyone else in that regard and offer the same safeguards that other companies do, and the first port of call is the pensions regulator… (TSC 2007, p.17-18)

Likewise, with the issue of using covenant-lite loans by private equity and the risks that might be associated with it, the private equity industry took the stance that this issue was the responsibility of the banks. This 'pass the buck' strategy was effective in framing the extravagant practices of private equity as the result of other actors' behaviour, such as banks in the case of covenant-lite loans and up-scaling of leverage. Also, this tactic highlighted the

existing regulatory structures already in place to monitor the various facets of private equity's activities, in particular the FSA.

The ultimate victory for the private equity industry becomes apparent in recommendations and policy changes adopted in the wake of the committee hearing. The Treasury committee's final report on the private equity industry agreed to review the implications for the HM Revenue and Customs of taper relief, treating 'carried interest' as part of capital gains tax and the use of debt in highly leveraged deals (TSC, 2007b, p.3-4). Recommendations for review are indeed a victory for private equity, as there is no mention of potential new regulation or policy change. In fact, the TSC seemed convinced by the arguments put forward by the industry in their admission that the structure of UK taxation treats all debt for investment in a particular way:

> The UK's tax system has long drawn a distinction between debt and equity, recognising them as different forms of finance. Interest payable on debt financing is typically considered to be an allowable business expense, whereas the return payable to equity holders is not as it represents the distribution of a company's profits. Many major tax systems adopt a similar approach, although they often apply restrictions on interest deductibility which are absent in the UK (Treasury Committee, 2007b, p.4-5).

In addition, the final report tasked the FSA with conducting a twice yearly survey of banks exposure to leverage buy-outs and to consider the potential for greater monitoring of covenant-lite loans (ibid, p.5). Again the Treasury Committee has taken on board private equity's argument that excess leverage and covenant-lite loans are the preview of the regulator and the responsibility of banks. This perspective leaves the large-cap funds' business model in tact as existing between various regulatory frameworks with no direct oversight of their business activities.

The policy changes ultimately adopted by the government, outlined in the Pre-Budget Report, reveal that the large-cap funds escaped the mediated scandal virtually unscathed. With the sub-prime mortgage crisis and the onset of the global credit crunch the tide had turned away from holding private equity to account. Instead, the clear fear was the potential macroeconomic effect of a slowdown in financial services. Fear that the entire financial services industry was in trouble translated into the government looking for new ways to provide additional aid to the sector, rather than new regulation. Moreover, the changes to tax policy adopted the private equity industry's stance that they should not be singled out and that any changes would affect all UK businesses.

Reforms to Capital Gains Tax, implementing a flat 18% rate for all business, and abolishing taper relief, is in line with the governments political commitment to establish a clear and fair tax system that is internationally competitive (TSC, 2007a, p.6). The Treasury committee goes on at great length to ensure that these reforms are not explicitly aimed at singling out the private equity industry: 'the Chancellor of the Exchequer's statement to the House of Commons clearly link the reforms of the capital gains tax regime to the aim of ensuring that the private equity industry pays a fairer share of tax, although the Government has denied that this was the primary motivation for the reforms' (ibid). In fact the Pre-Budget report express concern that these changes to the tax rules may be too hasty, or reactionary, and it cautions the government to consult more widely on the effects of reforming CGT and taper relief, even though consulting on changes to tax rates is not a common practice (ibid, p.2).

Throughout their testimony to the committee, the BVCA and large private equity funds fought against any notion of reform on CGT, claiming it would hurt the economy as a whole (since private equity follows the same tax rules as all business). Yet managing director of Duke Street Capital Peter Taylor claimed: 'I do not think a rate of 15 or 20% would be a material disincentive to entrepreneurs like ourselves to create value over the long term' (TSC, 2007,

p.73). In the wake of the publication of the Pre-Budget Report the Council of British Industry and various other business groups vociferously complained about the increase in CGT, while the private equity industry remained typically out of the public spotlight. This minor reform to CGT did not jeopardize any of the fundamental aspects of their business model. Moreover, profits distributed to GPs are still treated as capital gains. Even in the case of more simple reforms there was no direct action. Instead the industry was left to adopt a series of voluntary codes offered by the Walker Commission. Private Equity is still not legally required to disclose their portfolio of holdings or produce annual reports for the business they acquire. The reports produced by the Treasury effectively closed the book on the private equity industry, for the time being at least.

Conclusion

The mediated scandal surrounding the practices of Private Equity and its success in avoiding regulatory change during the summer 2007 was the trigger of this paper. To probe how this politically disorganised faction of the City of London managed to escape unhurt from the media frenzy and public scrutiny – an outcome that cannot be explained with reference to our common understandings of how business enterprises typically extracts policy concessions in British politics – was the task this work has attempt to fulfil. It was argued that private equity's victory, despite its poor performance in front of the Treasury Selected Committee, came as a result of its successful mobilization of existing ideological and structural conditions, which put the onus on the government to justify any regulatory or tax changes. The process was two-fold: firstly, the private equity industry challenged the government to adhere to its own political commitments to a clear and fair tax system; secondly, it worked on the line that private equity's business practices did not contravene the existing tax rules and that existing regulatory structures provided oversight of the constitutive elements of the industry's practices, even if the industry itself was not directly regulated.

The industry's ability to focus on the legality of their business practices and point out the unpredictability of changing the existing regulatory and tax structure was a crucial tactic. The government appeared to be convinced by these arguments, however, because they conformed to New Labour's, and the Conservative's, political commitment to reducing 'red tape' and ideological commitment to let the market in general, but the City in particular, to operate unencumbered by government intervention. The private equity may have unwisely picked fights with other industries within the financial services sector, but being part of the City offers special advantages because of its strategic position as the engine of economic growth and most internationally competitive sector in the UK economy. Therefore, in the end, no policy change presented itself that was realistically going to be implemented by a government, and Opposition, so firmly committed to fostering the financial services industry.

Recommendations adopted in the Treasury's final report clearly demonstrate the degree to which the government ultimately accepted the arguments put forward by the private equity industry. By putting the onus on the government to justify any changes to the tax or regulatory system, private equity successfully prevented any regulatory intervention. Time and again, the industry pointed out that they did not make the rules governing tax or regulation, and that the existing rules applied to all UK industries equally. In the case of taxation (tax relief on debt, taper relief and carried interest treated as capital gains), the government is committed to maintain a clear and fair tax system this precluded the option of adopting any changes adding new complexities to the tax code or single out any industry as an exception without facing a public scandal of its own. The existing structural and ideological conditions meant any attempt to directly address any of the issues relating to tax would ultimately require the government to fundamentally alter the form and intent of British business taxation policy.

Moreover, the private equity industry avoided any direct regulatory supervision by adapting its argument about taxation, namely that the existing structure was sufficient and any changes would need require some political justified. Private equity demonstrated that the constituent parts of its business practices have their own regulatory oversight and framework: the pension funds that provide the equity, the banks that lend the money, and the firms they purchase. In addition, the Financial Services Authority, the Bank of England and the European Central Bank all provide sufficient oversight of the overall financial services sector. The existing regulatory framework was not broken, and did not require a special form of regulation for the private equity industry. The only justification the government could offer to justify drawing up new regulations for the private equity would be the industry's recent growth in profitability and complaints from stakeholder unions. It appears the government was unprepared to make the effort, instead it opted for the 'insider' solutions offered by the private equity industry: voluntary codes and some additional research by the Financial Services Authority.

The government's reluctance is partly explained by the intervening event of the sub-prime mortgage crisis which hit world markets in August 2007. Perhaps not coincidentally, the issues brought up in the Treasury Select Committee about private equity business practices (i.e. excessive leveraging, covenant-lite loans and the potential systemic risk) turn out to be some of the endemic problems within the financial system. One could argue the excesses of the private equity industry were a symptom of the even bigger excesses of the financial system more generally. But the Treasury clearly did not see things this way. On the contrary, as the Pre-Budget Report shows, the biggest concern was protecting the financial services industry from further adverse effects of credit crunch. Over a year later, even as the true extent of the problems within the financial services sector are revealed, the government and the Opposition are united in their view that The City needs the state's support in nursing it back to health.

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[1] The ‘inner circle’ is the term coined by Useen to explain the new ties between different elites during the 70s and 80s. See USEEM, M. (1984) *The Inner Circle,* Oxford, Oxford University Press.

[2] Sir David Walker started as an Executive Director Bank of England during City revolution in the 1980s, from which he became the second chairman of Securities and Investments Board (SIB) to ensure regulatory changes were sufficiently implanted, from there he became Chairman of Morgan Stanley International and finally Senior Advisor at Morgan Stanley International before heading up working group set up by the BVCA on disclosure and transparency.

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