Pensions & Investment
Research Consultants Ltd
6th Floor, 9 Prescot Street
London E1 8AZ
Telephone +44 (0)207 247 2323
Fax +44 (0)207 7680 4081
Email info@pirc.co.uk
www.pirc.co.uk

Media Release
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PIRC Recommends No Vote at Betfair AGM

Illegal Dividends and Buybacks in 2011, 2012 & 2013 Raise Serious Governance Questions

PIRC, Europe's largest independent corporate governance advisor is recommending a No vote to reject the Annual Report of Betfair Group PLC at Thursday's 4th September AGM in London.

In its proxy report on the company sent to its institutional investor clients PIRC states that the company paid illegal dividends in 2011, 2012 and 2013, and with share buy-backs that it believes were similarly unlawful, a total value amounting to £60m is at stake.

The company says in its annual report page 113, Note 26 to the accounts:

"The Company has paid a final dividend for the year ended 30 April 2011 and interim and final dividends for the years ended 30 April 2012 and 2013 (the Dividends). The Company has recently been advised that, as a result of certain changes to the technical guidance issued by the Institute of Chartered Accounts in England and Wales (the ICAEW) in October 2010, the Company did not have sufficient distributable reserves to make those distributions and so they should not have been paid by the Company to its shareholders."

PIRC has been consistently critical of IFRS accounting standards (and UK GAAP copies, which applied in the case of Betfair) which does not deal with distributable profits and reserves, contrary to the legal requirement for accounts to give a true and fair view. PIRC has also questioned the validity of the ICAEW guidance 2010 as it is contradictory to the true and fair view requirement of the Companies Act in first instance.

However, given that the ICAEW guidance was issued in October 2010, well before the 30 April 2011 year end accounts and audit, this does not in PIRC's view explain why the illegal distributions were made much later in 2011, 2012 and 2013, particularly as the mistake was not a one off but repeated 5 times.

PIRC research shows that the amount by which profits were overstated in the accounts of Betfair Group plc was initially £134m (when the true position was a loss) and remains overstated by at least £154m.

'In PIRC's opinion if the accounts themselves were not an appropriate basis to declare a lawful dividend from, then the accounts did not give a true and fair view, and PIRC questions whether they still do, 'Managing Director Alan McDougall said.

'PIRC notes that shareholders have been asked in prior years to vote on the payment of dividends that in fact were illegal due to defective accounts. That makes the validity of the company's accounts themselves questionable as the key source of information for shareholders at the AGM to exercise class rights. Accordingly PIRC is recommending a No vote on a resolution to accept the entire Annual Report,' Mr MacDougall said.

For more Information:

Alan MacDougall
Managing Director, PIRC
M: +44 (0)7889 247871
E: alanm@pirc.co.uk

Andrew Whiley
Head of Communications, PIRC
M: 0791 874 7636
E: andrew.whiley@pirc.co.uk

Background Notes to Editors:

The law

Whether a company can make a lawful distribution is governed by two linked requirements:

- Section 830 CA 2006. Whether the company has sufficient distributable reserves to cover the distribution at the time the dividend/buyback is made, AND

- Section 836 CA 2006 settles the procedure as to whether any distribution can be made at all. The last public accounts ("relevant accounts") must show sufficient distributable reserves to justify the dividend paid, by reference to those accounts. Those accounts must give a true and fair view, subject to matters not material as to whether a distribution could be lawfully paid.

Betfair has breached both conditions but has only admitted publicly to the former

In PIRC's view, Betfair is in breach of both of the above requirements, but, has admitted the illegality by reference to the first criteria only.

It made distributions when it in fact had losses. It has since October 2013 rectified the deficit by paying up a dividend from a subsidiary.

However, it has not rectified the cause of the mistake which was defective accounts. Its accounts did not, and still do not, show the undistributable element of what appears in the accounts as distributable profit. Betfair used UK GAAP accounting standards which had imported elements of IFRS.

Betfair's position regarding the quality of its accounts is contrary to the true and fair view requirement per statute, case law and Opinion of George Bompas QC OF April 2013.

In Betfair's case, defective accounts have been the cause of an unlawful distribution. Directors declared, and shareholders voted on, what were in fact unlawful dividends.

On the basis of the Bompas Opinion, then, although Betfair may have made good the shortfall in distributable profits in the company, it has not changed its accounting; hence, all of any distributions are still unlawful as the public accounts do not give a true and fair view of the financial position and profit.

The Float

Betfair's share price was £15.50 on flotation in 2010 and is now £10.70, despite the illegal buybacks reducing the number of shares in issue. Press reports from the time[1] that the first dividends and buybacks were to help boost a lacklustre post flotation share price.

The numbers involved, total unlawful distributions of £80.3m

Betfair was floated in 2010. Its April 2010 accounts showed what appeared to be a profit and loss account reserve of £125.4m. Its April 2011 accounts showed what appeared to be a profit and loss account reserve of £134.7m. /p3

[1] Press http://www.theguardian.com/business/2011/jun/29/betfair-buyback-flotation-struggling-morana

Starting in October 2011 it then made illegal dividends and buy backs of £59.8m based on what appeared to be its profits in the 2010 accounts of £134.7m. The true “profit” was in fact a loss of £142k. It had no reserves at all to distribute (a breach of Section 830, as admitted); it was also in breach of Section 836 (not admitted) for having accounts not suitable to declare any dividend from.

It then paid illegal dividends of £11.2m in 2012 based on accounts that showed what appeared to be a profit and loss account reserve of £82.1m. The true position was now a loss of £651k plus the deficit of £59.8m due to the prior illegal distributions, i.e. a £60.5m deficit was the true position.

It then paid illegal dividends of £9.3m in 2013 based on accounts that showed what appeared to be a profit and loss account reserve of £77.5m. The true position was now a loss of £1.6m plus the deficits due to the prior illegal distributions of £59.8m and £11.2m i.e. a £72.6m deficit was the true position.

The illegal distributions totalled £80.3m, by which time Betfair was in total profit and loss account deficit of £81.9m.

Conflicts of interest/unresolved questions

Betfair’s directors stated in the April 2014 annual report accounts that Betfair had adequate internal controls for that year. That was despite recognition an unlawful distribution had been made in that year in question October 2013. (There is no reference to the unlawful distribution, other than in Note 26 to the accounts.) The audit committee directors also state that they were happy with the performance of the auditor, KPMG, who have been auditors prior to and since flotation.

Betfair’s directors and auditors have confirmed that the April 2014 accounts give a true and fair view. That is despite the fact that what appears to be a profit and loss reserve of £333m is still overstated by at least £154m, i.e. the accounting overstatement has not been adjusted <u>nor disclosed</u>. All that has happened is a receipt of a subsidiary dividend of £182m to cover the actual deficit. On the basis of the Bompas Opinion, Betfair’s accounts are still not a proper basis to declare a dividend from - distributions are still unlawful in whole.

When a distribution is unlawful, then it remains the property of the company as it is deemed not to have been able to have been made. It falls as a liability of:-

- the directors personally
- the members

The members of a public company where they did not know of the problem have a statutory right not to be pursued by the company. However, that does not prevent the directors pursuing the shareholders where the company pursued the directors.

In addition, where a member is a director in receipt of a dividend there is no defence that they could not have reasonably not have known. Betfair had two large director shareholders on flotation who were in receipt of substantial dividends

Directors when liable to the company for an unlawful distribution may have recourse to the auditors where the default was due to an accounting problem due to their negligence. Betfair has not disclosed any facts about the culpability of the auditors (KPMG).

Previous Reporting

Betfair to buy back £50m shares months after its flotation
Guardian 29th June 2011

Investors demand action on IFRS failings after problems at online gambling firm
IPE Europe 14th August 2014

Legal Opinion
Banks Post Mortem- Bompas QC Opinion- November 2013

PIRC Ltd 2nd September 2014

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