RIGSREVISIONEN

Extract from the report to the Public Accounts Committee on the financial position of TV 2 Danmark A/S

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I. Introduction and main findings

1. TV 2 Danmark A/S (public broadcasting company) reported a substantial deficit of DKK 213.5 million for the year ended 31 January 2007. In mid-May 2008, TV 2 informed the Ministry of Culture that the company had serious liquidity problems. Subsequently, in June 2008, the Ministry of Culture approached the Finance Committee and in a confidential document the Ministry requested endorsement of a temporary government loan to TV 2.

2. At some point during the processing of the document, the Finance Committee decided to ask the Public Accounts Committee to consider carrying out an examination of the financial position of TV 2. On 20 August 2008, the Public Accounts Committee asked Rigsrevisionen to conduct a major study of the TV 2 Danmark A/S finances. The Public Accounts Committee wanted the study to clarify, based on a number of specific questions, the development of the TV 2 finances and the causes of the requirement for a temporary government loan.

3. The overall objective of the study was 1) assessment of the financial management of TV 2 performed by the management and its board of directors, and 2) assessment of the causes of the negative development of the financial position of TV 2. Based on the questions formulated by the Public Accounts Committee, Rigsrevisionen has addressed the following issues:

- Has the development in the finances of TV 2 developed in a satisfactory manner since the company was incorporated as a limited liability company in 2003?
- Has management's handling of the TV 2 group finances been satisfactory?
- Has management's handling of selected business activities and agreements been satisfactory?
- Has the Ministry of Culture, which owns TV 2, exercised adequate supervision of the finances of TV 2?

On the basis of a new strategy, TV 2 Danmark A/S launched a number of business initiatives in 2006 and 2007 – among these TV 2 News A/S, TV 2 Sport A/S, TV 2 Radio A/S and New Bizz Areas (a business unit whose operations included publishing, events and lectures).

MAIN FINDINGS AND CONCLUSIONS

In the course of 2007, TV 2 ran into financial difficulties and was forced to apply for a temporary government loan. The difficulties were caused by generally unsatisfactory financial management by the management and board of directors at the time.

The executive management at the time had launched several liquidity demanding initiatives over a short period of time from mid 2006 – mid 2007 based on unrealistic budgets and supported by inadequate information. Some of the activities have since been closed or trimmed down, whereas others generated profits in 2008. Overall, the launch of these projects had a negative impact on the operating profit and cash flow situation of TV 2 in 2007. The then board of directors was largely uncritical to the budgets, the new initiatives and the general development of the finances of TV 2 and thereby failed to live up to its supervisory duties.

Generally, the Ministry of Culture has based its supervision on the principles provided in the publication ”Staten som aktionær” (The Shareholding State). When TV 2 made several liquidity-demanding investments, and the Ministry was aware that the financial framework set for TV 2 as a limited liability company did not allow for investments of such magnitude, the Ministry should have enquired into the financial impact of the proposed projects and whether they could be kept within the financial framework of TV 2. Last, the Ministry of Culture should have exercised a more active ownership of TV 2 when the Ministry learnt early in 2008 that the business management of TV 2 in 2007 had been reprehensible.

This overall assessment is based on the following findings:

The equity capital of TV 2 was satisfactory for operating on the basis of the premises laid down in its memorandum of association when the company was incorporated as a limited liability company in 2003. Generally, TV 2's financial position was satisfactory until, and including, 2006. TV2 did not run into financial problems until 2007, when it had an operating deficit and a substantial increase of debt, and thus suffered deterioration of its solvency.

- The equity capital of TV 2 was satisfactory for operating on the basis of the premises laid down in its memorandum of association when the company was incorporated as a limited liability company in 2003. The memorandum of association did not include plans for TV 2 to launch more large new investments projects and initiatives. External expertise was brought in when the company was incorporated in 2003 and recapitalized in 2004, and the assessment of the capital requirement was based on the same principles that a private investor would adhere to prior to making a similar investment.

- In the years 2003 – 2006, the financial development and position of TV 2 was satisfactory; the company generated a profit, the level of debt was stable and the solvency ratio was acceptable. In 2007, the solvency deteriorated, short-term debts rose significantly, and the company reported a substantial operating deficit. The financial difficulties can be traced back to 2007 and the subsequent period, but the problems must also be considered in the context of decisions made in 2006 to launch new activities.

- The government aid granted to TV 2 has not had any impact on the operating results of the company, but it has impacted its loan facilities.

Management's handling of the finances of TV 2 has been very unsatisfactory and has not lived up to the principles of good public ownership and management. The executive management at the time launched several liquidity-demanding initiatives late in 2006 and in 2007 based on unrealistic budgets and supported by inadequate information. In combination with declining advertising sales, these initiatives had a negative impact on the financial position of TV 2 in 2007. The then board of directors did not ensure that budgets were supported by adequate information. Neither did the board of directors in 2007 take the appropriate steps to curb the negative financial development.

- The operating profit of TV 2 was in 2007 considerably lower than expected, primarily because revenue generated by sale of commercials was down on budget, and depreciation and amortization were extraordinarily high. In addition, TV 2 made significantly more investments than planned in 2007. These investments and the shortfall in operating income contributed to increasing the liquidity problems of TV 2, and the company's debt increased beyond the expected level in 2007.

- In November 2006, the management at the time worked out an unrealistic budget for advertising revenues in 2007. The budget was based on the assumption that advertising revenues would increase steeply despite a stagnant advertising market. The board of TV 2 at the time was uncritical to the budgeting and the assumptions upon which the budget was based, and thereby also to the risk inherent in approving the budget.

- In compliance with the management instructions of TV 2, the then management informed the board on a monthly basis of variances to budget and decreasing liquidity. On the other hand, and contrary to the management instructions, the management did not inform the board of directors of the development of the TV 2 debt and the TV 2 building projects.

- In August 2007, when the half-year accounts were prepared, the management launched a cost-cutting plan. The board enquired on several occasions into the financial situation of the company and received overly positive reports from the management. But the board was uncritical to the reports received and did not take the appropriate action in response to the warning signals concerning the shortfall in operating profit and decreasing liquidity.

- The auditors of TV 2 worked out an auditor's report in November 2007 from which it appeared that they had reviewed and assessed the overall internal controls of TV 2. Internal controls comprised, for instance risk management and financial reporting. The auditor's review and assessment did not result in any qualification. In March 2008, the chairman of the present board of directors of TV 2 considered it censurable that the auditors had not earlier called attention to the substantial variance between the actual and budgeted result for 2007. According to the chairman, the auditors could have mentioned this in the auditor's report from November 2007. Rigsrevisionen agrees with this assessment and is of the opinion that the auditor has been too passive. The auditor should have pointed out to the board at the time that the financial position of TV 2 was deteriorating, as it appeared, for instance from the monthly finance reports prepared by the management of TV 2. In April 2009, the TV 2 general assembly decided to appoint another auditing firm.

TV 2 launched several new business projects in the second half of 2006 and during the first 6 months of 2007. Several of these projects were launched on the basis of inadequate information provided by the management at the time. The then board did not take steps to ensure that the basis for decision-making was improved. Furthermore, the management had also launched projects that had not been authorised by the board. Some of the new business projects launched by TV 2 have since been terminated or continued at a reduced level of activity. Still, two of the largest, new business projects generated profits in 2008.

The then management's and board of directors' handling of the TV 2 building project on Teglholmen was censurable as was management's handling of selected distribution contracts.

- The management's handling of the launch of TV 2 Radio was unsatisfactory. With the support of the board at the time, the then management of TV 2 worked out a basis for decision based on optimistic estimates of number of listeners and advertising income. Subsequently, it was established, that TV 2 Radio did not live up to the projected radio ratings and advertising income.

- The decision to launch New Bizz Areas and many of the other business initiatives was made on the basis of inadequate information provided by the then management, and the information was based on rough estimates rather than on market-based financial analyses, etc. The board at the time was largely uncritical toward the information providing the basis for the activities. The activities launched did not contribute to improving the group's financial position, which was one of the objectives of launching the projects.

- Rigsrevisionen finds it particularly unsatisfactory that the temporarily appointed managing director of TV 2, in conflict with the TV 2 provisions regulating the powers to bind the company, entered a supplementary agreement to expand a lease on Teglholmen. The agreement does not cap costs related to the refurbishment of the lease. The agreement is a financial burden on TV 2, as it has doubled the company's annual operating costs per square meter.

  Up until the autumn of 2006, the board of TV 2 at the time enquired into and was informed by the management of the expansion and refurbishment of the lease. Since 2007, the board was only briefed orally by the management. In 2007, the information provided by the management touched only on occasion upon finances. In the second half of 2007, the management did not keep the board informed about the project. Rigsrevisionen finds that the information provided by the management to the board about the building project in 2007 was too sparse and in some instances misleading. However, Rigsrevisionen is also of the opinion that in 2007 the then board of directors was inactive in relation to the building projects. For instance, the board of directors did not ask to see the agreed financial statements.

- In the autumn of 2007, the temporarily appointed managing director of TV 2 entered several agreements on distribution of TV channels.

  Based on the material available, Rigsrevisionen is of the opinion that the agreements are intransparent; they do not seem to be commercially founded and financially they do not seem to benefit TV 2. Besides, some of the agreements are extraordinarily brief. Rigsrevisionen has not, based on the sparse written material, been able to make a final assessment of the agreements, including whether they will have adverse effect on the financial position of TV 2.

  Rigsrevisionen has informed the owner of TV 2, the Ministry of Culture, about the agreements. The Ministry has indicated that when the final report is available, it will review the information on the agreements provided by Rigsrevisionen and subsequently contact the board of TV 2 to discuss whether further examinations or initiatives relating to the agreements will be required.

As sole-owner, the Ministry of Culture is responsible for the overall supervision of TV 2. This supervision is based on the principles provided in the publication "The Shareholding State". As part of the supervision, the Ministry has been involved in the development of the TV 2 strategy for 2006 and the Ministry has had ongoing discussions with the company about whether specific projects were in compliance with the objective set for TV 2. When TV 2 made several liquidity-demanding investments within a short time span, and the Ministry was aware that the financial framework of TV 2 as a limited liability company had not been established to accommodate investments of such magnitude, the Ministry should have asked for information on whether the projects collectively could be kept within the financial framework of the company. Furthermore, the Ministry of Culture should have exercised a more active ownership of TV 2 when the Ministry learnt early in 2008 that the business management of TV 2 had been censurable the preceding year.

- The Ministry of Culture has established an overall supervision based on the principles provided in the publication the Shareholding State. The Ministry of Culture appointed a board of directors who had the overall responsibility for the financial position of TV 2. Furthermore, the Ministry took an active role in the strategic considerations concerning the TV 2 launch of several new projects, and together with the Ministry of Finance, the Ministry of Culture prepared a memorandum on the execution of government ownership. According to the Ministry of Culture, the overall framework for the strategy and performance of TV 2 laid down at the meeting in March 2006 provided the basis for the Ministry of Culture's supervision of TV 2 in the subsequent years.

- The Ministry of Culture and TV 2 have discussed the launch of specific projects on an ongoing basis, for instance in connection with the strategic planning in 2006 and the changes proposed to the strategy in 2007. Knowing that TV 2 was making several liquidity-demanding investments, the Ministry should have asked for information as to whether the projects collectively could be financed within the financial framework of the company in relation with the strategy discussions. The activities were launched in the period mid 2006 to April 2007, i.e. within a period of less than 12 months. At the same time, the Ministry was aware that the financial framework of TV 2 as a limited liability company had not been established with a view to making major new investments. Furthermore, in the autumn of 2007, TV 2 presented its proposal for a new strategy including more new projects and an ambitious objective to double the revenue.

- Last, Rigsrevisionen finds that the Ministry of Culture has not so far been sufficiently active in its efforts to clarify whether there was reason to look into decisions made by the former management of TV 2 when the Ministry learnt early in 2008 that the management of TV 2 had been censurable the preceding year.