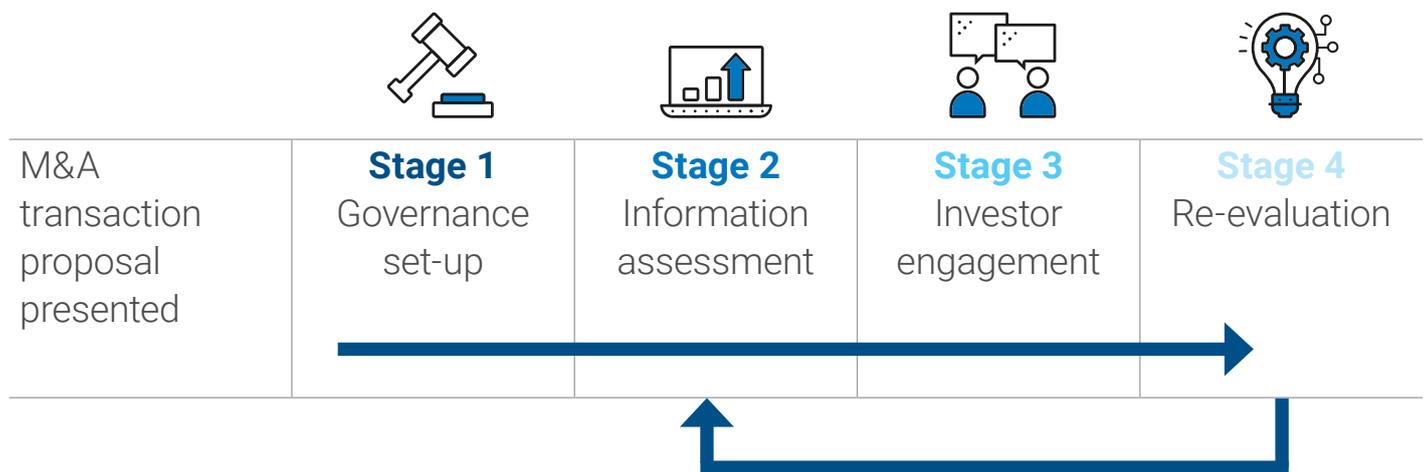


A guide to mergers and acquisitions: Board oversight

Mergers and acquisitions (M&A) are a key feature of capital markets that provides companies with the opportunity to enhance and generate optimal returns to investors. However, large transformational transactions also carry significant risks and often do not generate the long-term value promised.

For many companies, transformational M&As are not an everyday occurrence, therefore having a clear plan and structure in place in advance of any proposal can help guide board debate.

Board governance framework for M&A



Governance set-up

Inform early and manage conflicts

The board should be given sufficient time to assess the transaction to allow for the full consideration of all the appropriate information to take part in discussions and raise questions about the transaction.

If a director is conflicted (directly or indirectly in the broadest sense), Legal & General Investment Management (LGIM) would expect full disclosure of the nature of the conflict and the board to take steps to remove or mitigate the conflict.

Establish an independent oversight committee

For large transactions, additional scrutiny and oversight can be helpful to keep the transaction on track and focused on delivering long-term value for investors. The function of the committee is to enable clear and objective deliberations to be held between committee members (independent non-executive directors, or NEDs) without any perceived bias being present. Directors who are conflicted should not sit on this independent committee.

Obtain separate independent advice

In terms of information being provided to the board on the transaction, this would mainly come from management and corporate advisers. However, both may be incentivized to see the transaction completed, either directly through completion fee structures or indirectly.

We therefore see benefits of independent advisers being appointed to report to the board who are remunerated on a flat-fee basis and not connected to the transaction.

Investors expect the substance of such independent advice to be disclosed in relevant documentation such as the prospectus. Sufficient detail should be given to enable investors to be comforted that independent non-executive directors have challenged the merits of the transaction.

Information assessment

Evaluate the metrics

Companies should continuously evaluate the expected long-term returns of the transaction and closely scrutinize potential value creation based on business fundamentals. This process is particularly important as M&A timelines may be long and changes in the market may invalidate assumptions which initially supported the deal.

The board should carefully examine the metrics used to justify the case of the transaction, taking care to consider and communicate the performance benefits beyond just short-term earnings enhancement or immediate synergies.

Integrate the culture

Understanding the cultural fit between the two organizations is essential for the transaction to be successful. The board should be comfortable to not proceed with a transaction if the cultural integration risk is too high. The board's ongoing oversight and monitoring of the specifically-designed plans to assimilate cultures is critical. Appropriate people-related metrics and objectives aligned to the final desired culture should be defined and regularly monitored during and following the transition.

Consider post-transaction listing options

If the transaction involves changes to the listing structure, the listing options of the company after the transaction should be fully considered. This includes taking note of jurisdiction and index inclusion as long-term shareholders would like to continue to participate in the growth of the company.

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Investor engagement

Board chairs and NEDs to meet investors without management present

The board chair and NEDs should make themselves available to engage with investors (both equity and debt) to discuss the transaction. This will allow investors to better understand the governance process undertaken. In addition, the board chair will have the opportunity to hear directly from investors their views of the transaction and discuss any issues or areas of concern.

All significant transactions should be approved by shareholders

In all cases, LGIM expects a General Meeting to be held to approve significant transactions even if the company operates in a market where it is not the norm to put such resolutions to a shareholder vote.

Remuneration and other governance arrangements connected with the transaction should be set out as separate items for approval by shareholders on the meeting agenda (i.e. not bundled). This is so investors are able to express their views on the resolutions without jeopardizing the whole deal.

Re-evaluation

Post M&A board review

It is important that boards undertake a formal review of their internal controls and due diligence framework after the M&A process has been executed. By gaining an insight into lessons learned, companies will be able to further strengthen their procedures over time.