



New England Chapter

October 14, 2008 Session  
Highlights of the Presentation  
“The Board’s Role in M&A”

## The Board’s Role in M&A

What is the role of the board of directors at a public company when a merger or acquisition is proposed? That question was the subject of the October 2008 Boston breakfast meeting of the New England Chapter of the National Association of Corporate Directors (NACDNE). First, using a fictional case study created by Ellen Richstone, a director of several companies and EVP of Luminus Devices, and Hugh Taylor of Newbury Piret & Co., attendees at the meeting played the role of either a) board members at a company proposing an acquisition or b) board members at the company that is the target of the acquisition proposal.

After attendees considered the fictional scenario, a panel of experts discussed the topic and the case study. The distinguished panel consisted of: Sally Crawford, John Kassakian, Christopher Oddleifson and Hugh Taylor. Crawford is a director of Hologic Inc. who was on the board of Cytoc when it was bought by Hologic; she is also a director of EXACT Sciences, CominatoRx and Universal American Corporation. Kassakian, a professor of electrical engineering at MIT and the director of the MIT Laboratory for Electromagnetic and Electronic Systems, is currently on the boards of ISO New England and the Marvell Group, as well as on the corporate advisory boards of Tyco Electronics and Lutron Electronics. Oddleifson is currently president and CEO of Rockland Trust Company and its parent, Independent Bank Corporation. Taylor is Managing Director at Newbury Piret & Co.

Here is the fictional case study that attendees and the panelists discussed.

### **THE FICTIONAL CASE STUDY: A PROPOSED DEAL**

Innovative Technology’s President had just been approached by the President of Strategic Foreign Corp, which offers to purchase Innovative for Strategic’s stock at a 20% premium over Innovative’s close yesterday on the NYSE.

*Innovative Technology (“Target”)*: Manufactures and sells \$500M/ year of its engineered products in twenty countries, with 60% sold in the US. Over the last two years, it has operated profitably with a 15% growth rate; over the last 10 years, its growth has been over 30% with even larger profits. Current cash flow is positive but not sufficient to support both high internal growth and the cash acquisitions that the Board and management have agreed to pursue to consolidate market share; there are two signed nonbinding letters of intent for these acquisitions, one contingent on financing. The stock is down 20% from 12 months ago, 35% from three years ago. The new CEO has tightened sales and distribution and identified the increased market share strategy endorsed by the Board; the CEO believes that the plans will generate growth at 40% per annum, but the Board recognizes that there is considerable execution risk in the plan.

*Strategic Foreign Corp (“Acquirer”)*: Manufactures and sells \$600M/year of its engineered products that are complementary to those made by Innovative, with 75% of sales in Europe. Strategic’s shares are listed on the London Stock Exchange. Its balance sheet shows cash and modest levels of debt. In the past Strategic has also been known to reconfigure acquired companies, keeping pieces, selling off non-core assets and laying off redundant personnel. Its profitability and growth rate has been slightly higher than Innovative, and most of its revenues and earnings are denominated in Euros.

### **The panelists’ comments on the fictional case study:**

For the target company, the level of effort that’s required to evaluate an offer like this is often underestimated, Kassakian observed. Forming a three-person subcommittee of the board to consider the issue is an excellent idea, he said — as long as members of that subcommittee understand it will be almost full-time work during the process. Kassakian added that probably the biggest reason mergers fail is that acquirers don’t understand what they’re buying. The acquirer, he observed, has a vision of the benefits of the acquisition, but the benefits often seem to be better in that vision than they are.

As he discussed the fictional case study, Oddleifson noted that the two companies appear to be a good strategic fit. However, he said, “This is not a bona fide offer.” There are a lot more details to an offer than a 20% price premium, Oddleifson explained — and the board is within its rights to brush this proposal off. However, he added, “I do think this is a bit of a wake-up call for the target company,” he said. Is the 40% growth the current CEO is proposing real? The board of the target company has to have a clear sense of the company’s strategy; then it will have a better sense of whether a 20% premium is good or not.

Crawford noted that because the offer in the hypothetical case study is a stock offer rather than cash, that gives the board a lot more flexibility in how it responds to the offer. She expressed agreement with Oddleifson and added that there’s not a need right now to disclose the offer publicly or throw this into an auction. If the board were to look at this offer, Crawford said, it would have to look at the stock of the acquiring company and really size up its management.

Crawford also said that unsolicited offers rise as stock prices fall and she recommended a readiness approach for boards. She explained how, when she was on the board of a company whose stock was trading at a comparatively low price, the board devoted part of every meeting to topics that would prepare them in case an offer was made for the company — such as the topic of fiduciary duty. Unsolicited offers, she observed, become like “very elaborate poker games” or sophisticated chess matches.

### **From the Question and Answer Session**

**Q. After an offer like this, what’s the next thing you say? What’s the next thing done by the target company in response?**

**A.** “Externally, it can be ‘No, thank you,’” Oddleifson said — given the informal nature of the acquiring firm’s proposal. Usually, Crawford observed, the first round is to say ‘thanks, but no thanks’. Kassakian recommended asking the potential acquirer to submit a formal proposal if they are really serious.

**Q. At what point should an offer like this be made public?**

**A.** Assuming there are no leaks, Oddleifson said, the notification happens when a definitive agreement is signed. However, if there are rumors that are influencing stock price, seek out your counselors; you might have to preannounce.

An offer is a wake-up call, and you’ve got to anticipate what comes next, Crawford said. She described the case of a company that did not want to be sold, and the board said “no” four times to the potential acquirer — and the acquirer took the issue to shareholders and made a tender offer. “Sometimes, it starts

to have a life of its own,” she explained.

- Q. Assume you are the board of the potential acquirer in this example. Suppose you knew about this proposal before the conversation between the two presidents occurred, but you have not done a very thorough analysis of it. What should be the next step for the acquiring board?**
- A.** Crawford described how one board on which she served had a Finance Committee that screened all financial transactions — and this would be one. Kassakian noted that, for an acquiring company, the big problems come after the acquisition. He raised several questions for consideration: How are you going to integrate this acquisition into your organization? Are the two sales forces compatible? Are the two cultures compatible? And Oddleifson offered this question for consideration: Tell me how we are going to retain the top customers of the acquired organization and the employees we want to keep.

Taylor noted that the potential acquirer has made an all-stock offer, and the likelihood is that that offer is going to be rejected. If the acquiring company has to go to the capital or debt markets to raise capital for this transaction, what are the implications of that? Does it make sense to pay the price? Can the acquiring company finance it?

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For more information about the New England Chapter of NACD, please contact [info@nacdne.org](mailto:info@nacdne.org).

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