

## ACCOUNTABILITY AND TRANSPARENCY

Are Your Corporate Governance Practices Putting You at Risk?

### Evaluating Acquisitions in the Boardroom

#### CO-SPONSORS



**D.F. KING**



Morgan Stanley

#### IN-KIND SPONSORS



## Evaluating Acquisitions in the Boardroom

November 6, 2014

### Panelists

- **Peggy Kelsey**  
Modine Manufacturing Company
- **Rebecca Newman**  
Aon plc
- **Andrew Schiesl**  
Gardner Denver, Inc.
- **Hugh Sullivan**  
Morgan Stanley & Co.
- **John Wilson**  
Foley & Lardner LLP

## Pre-Acquisition Discussions and Development of Acquisition Strategy

- Board involvement in the acquisition process should begin before any specific acquisition is proposed
- In pre-acquisition discussions, the Board and management should discuss the company's acquisition strategy, including acceptable transaction and risk metrics, potential acquisition targets and opportunities, risks associated with certain types of acquisition targets, and potential funding sources
  - The Board should make its expectations regarding the acquisition process clear (e.g., when the Board expects its involvement to begin and the type and level of information that the Board expects to receive)
- The company's acquisition strategy may include the engagement of a buy-side financial adviser, or parameters for determining if and when the company will engage a financial adviser
  - Prior to engaging a financial adviser, the Board must consider any actual or potential conflicts of interest
  - The Board should be directly involved in establishing the terms of the engagement

©2014 Foley & Lardner LLP

## Pre-Acquisition Discussions and Development of Acquisition Strategy

- By having an acquisition strategy in place and by proposing acquisitions that are part of that acquisition strategy, it will be easier for management to get the Board "up to speed" when an acquisition opportunity arises
- Pre-acquisition discussions will provide the Board and management with a common framework for evaluating proposed acquisitions
- Management should periodically update the Board regarding transaction metrics in the industry so that when a "good deal" comes along, the Board is aware of recent transaction metrics and can make an informed decision more quickly
  - This practice is also beneficial in the event that management proposes a transaction that is not completely in line with all aspects of the company's acquisition strategy

©2014 Foley & Lardner LLP

## Evaluating Proposed Acquisitions

- When evaluating a proposed acquisition, the Board must be mindful of, and act in accordance with, its fiduciary duties:
  - Duty of Care – Requires directors to inform themselves of relevant and available facts and, so informed, to act with due care
  - Duty of Loyalty – Requires directors to put the best interests of the company and its shareholders over those of the directors
  - Business Judgment Rule – Protects Board from judicial scrutiny so long as Board decisions are made in good faith by disinterested directors exercising their duty of care
- The Board must:
  - Ask the “tough questions”
  - Maintain the appropriate level of skepticism
  - Help to identify, evaluate and address the key risks
  - Determine whether the company should move forward with a proposed acquisition.

## Evaluating Proposed Acquisitions

- Among other transaction-specific issues, the Board should consider the following:
  - How does the proposed acquisition fit into, support and/or advance the company’s acquisition strategy?
  - What benefits will the company realize from the proposed acquisition?
  - Is the proposed acquisition the best use of the company’s resources?
  - What assumptions are being used by management and/or the company’s financial adviser in evaluating and/or valuing the proposed acquisition? Are those assumptions realistic?
  - What projections are being used by management and/or the company’s financial adviser in valuing the proposed acquisition? What is the basis for those projections?
  - What are the risks associated with the proposed acquisition? How can those risks be mitigated / addressed? Consider business risks, as well as legal / litigation risks related to process, structure and transaction terms.
  - What are the benefits to be received by the company from the proposed acquisition, and will the proposed acquisition increase shareholder value?
  - Is the structure of the proposed acquisition the best structure for the company? Would another structure be more beneficial to the company?
  - What synergies can be achieved through the proposed acquisition? How will those synergies be achieved? When will those synergies be achieved?
  - Would it be appropriate to use data analytics and/or social media analysis in evaluating the acquisition target?

## Evaluating Proposed Acquisitions

- Board action to evaluate and/or approve a material acquisition should be taken at an in-person meeting of the Board, and the meeting agenda and materials should be provided to the Board sufficiently in advance of the meeting
- Among other things, directors should consider and/or review the following when meeting to take action on a material acquisition:
  - Fiduciary duties
  - Summary of material contract terms and copy of purchase agreement
  - Negotiations to date and material open issues
  - Extent and nature of business and legal due diligence review and any material due diligence findings
  - Valuation of the business being acquired
  - Fairness opinion of financial adviser, if applicable
  - Management recommendation
  - Director indemnification and D&O insurance coverage and limitations

©2014 Foley &amp; Lardner LLP

## Evaluating Proposed Integration Strategy

- Because the success or failure of an acquisition often relates to the company's ability to integrate the acquired business, the Board's evaluation of an acquisition should focus heavily on management's proposed strategy for integrating the acquired business
- In considering the proposed integration strategy, the Board should consider the following issues:
  - Who is responsible for the implementation of the integration strategy? Will a specific team be formed for this purpose? (It is important that someone has a vested interest in ensuring that the integration is successful.)
  - Will key employees of the acquisition target be retained to assist with the integration process? Have steps been taken to retain such key employees? Have those steps been successful?
  - What business issues must be addressed in integrating the acquisition target? How will those business issues be addressed?
  - How long is the integration process expected to take? What is the proposed timeline?

©2014 Foley &amp; Lardner LLP

## Evaluating Completed Acquisitions

- The company's acquisition strategy should include a process for measuring / evaluating the success of each acquisition
  - This process should focus on whether certain key metrics have been met
- If an acquisition fails, it is often a result of internal factors, such as lack of cohesion, conflicts, and failure to integrate the acquired business
- In most cases, if an acquired business is well integrated with/into the existing business of the acquiring company, the acquisition will be considered successful