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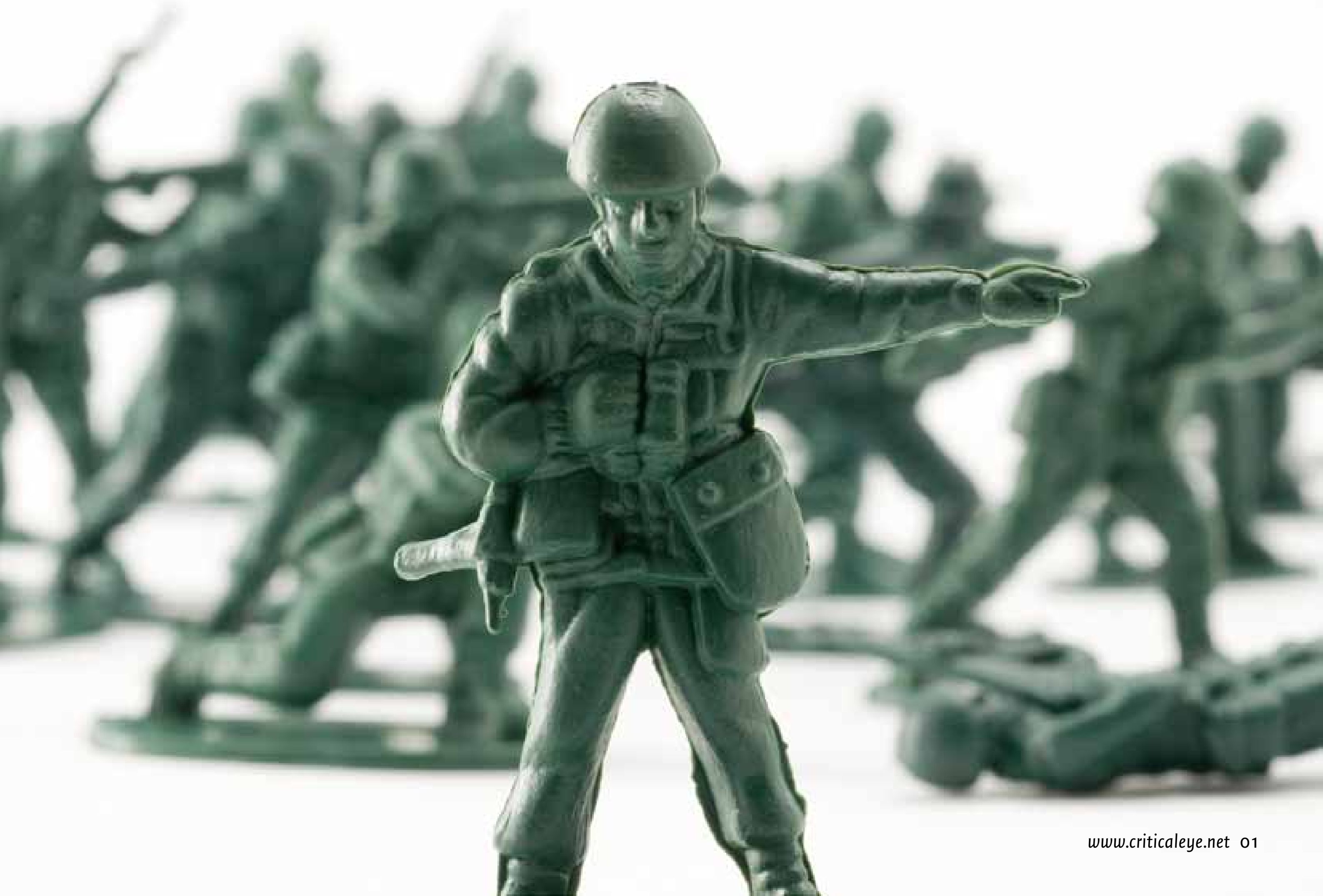
WAR GAMES

The default setting for chairmen changes quite dramatically during a takeover. **Steve Marshall**, *Chairman of Balfour Beatty plc, outlines how success is often governed by a Chair being able to manage personal conflicts and seeing the bigger picture*



The stresses exacted on a publicly listed business during a takeover frequently require the non-executive chairman to shift from the default passive mode and adopt a more active presence. Certainly you must never threaten to undermine or become the CEO, but you should actively clamber into the front to sit alongside the driving seat.

If someone's making an offer for your company you must be intensely involved with all the key stakeholders. You must be visible and seek to drive a board-centric process. You should seek to get a good feel for the type of people involved in the bid team, too, and be prepared for the broader impacts when the whole environment shifts. Your involvement with advisors will also move to a different plane.

No matter what happens during a takeover bid, the chairman and the board have three essential deliverables:

1. **Shareholder value.** You should emerge with a solution that maximises and/or preserves the value of your company to the best of your ability, requiring judgment that balances short and long-term concerns.
2. **Stakeholder engagement.** The outcome must be seen to be delivering maximum shareholder value: internally, the rigour and transparency with which the board conducts its processes and decisions may require justification; externally, the quality of the dialogue you have with key stakeholders will dictate the degree to which your recommended course is accepted (or not).
3. **Business return.** You must do the right thing by the business and the people in it, requiring you to weigh up the short/long-term perspectives and other alternatives, which aren't all necessarily attractive.

Good Corporate Governance plays its part, but the frameworks and requirements of the Code and the other continuing obligations that you have as a listed company are actually quite effective in improving the way companies and boards function.

Behaviours of key stakeholders can change as a bid develops and the Chairman must observe, manage and be savvy around the following three areas:

- **Human conflicts** – whether real or perceived in the board.
- **The board** – its constituents will require direction (not manipulation).
- **Advisors** – they must be of ultimate benefit to the company (not just themselves).

Beyond the nitty-gritty of governance, it is the behavioural areas of management in which the chairman must excel

Beyond the nitty-gritty of process and governance, however, I believe it is the human and behavioural areas of management during a takeover in which the chairman must excel.

MANAGING CONFLICTS

In any given takeover situation, the chairman of the targeted business must swiftly crystallise the best and worst outcomes for every key player in the boardroom. Independence is central to Corporate Governance best practice, but we are all human. I would challenge anyone that's been involved in a transaction who doesn't agree that we work from the selfish side out. Whatever your interest, there comes a point early-on where one thinks, what's the impact of this transaction on me?

That's not to say that we aren't capable of putting this aside. And, ultimately, we shouldn't let it cloud our broader judgment. The principle requirement for a chairman in a takeover – or indeed any – situation is therefore to know the board, know the individuals and, simply, observe behaviours.

Above everything else, you must get closer to your chief executive. Of course, you should already have a close relationship with him/her. But, particularly in a takeover situation, their attitude is absolutely pivotal to the outcome, so you must attempt to get inside their head and attune to their thinking.

Chief executives new in the job, that feel the company is being snatched from under them before even having a chance to prove their ability, might be more likely to stubbornly object to what could be a reasonable offer on the table. As chairman, you must understand that body language.

For example, if you've got a CEO who is well into a second term (in presidential parlance), and he/she is probably going to move out in a year or so anyway, there's really nothing more attractive for him/her than taking a nice, big payoff – with a degree of credit for handing the company on, too. As that CEO, are you really going to fight for that last 15 pence at the risk of the whole thing falling over?

Of course, you should never make rash judgments. But you need to be cognisant of what's driving the behaviours and, where possible, spot the inconsistencies, confront them and compensate for them. In these situations, it's easy to fall into the trap of assuming that anything the executives say is biased and anything the NEDs say is neutral. The reality can be markedly different.

Another example: I once knew a sexagenarian non-executive earning £40,000 a year who was irrationally against an offer for the company. It was his last plc directorship and he didn't want to see it topple over. You wouldn't think it possible, but it happens – you are presented with every shade in these situations and it doesn't necessarily align with roles or responsibilities, rather, it's about people.

A takeover is one of the few situations where the chairman needs to take a lead role with shareholders

BOARD CONTROL

As chairman, you have to be emotionally neutral to whatever outcome makes sense for the company and the shareholders. Sure, you can be proud of your company and fond of the people, but if you are emotionally involved you will not be able to do your job effectively.

Board unity is essential. If you have the executives outside the loop rather than hands-on and close to the tensions, it's not a happy place to be – and it may hamper your chances of delivering a value-maximising outcome.

To help moderate the more over-zealous opinions and keep the board cohesive, the chairman should focus on:

1. **Trust.** He/she must drum into the board its responsibility to demonstrate its fiduciary duties both to the company and to the shareholders, present and future. It's a great way of bringing people into line and stopping shortcuts. Your advisors can be incredibly helpful in reminding the board that this is its central focus.
2. **Rigour and process.** He/she should be relentless in insisting on the importance of supporting analysis, such as the board's paper trail, full minutes of the discussions and decisions of the board, advisors present with the board and the comments and responses to questions. Unusual questions should be noted and responded to openly – a good company secretary will be invaluable.

ALIGNING ADVISORS

Advisors are much maligned yet often fabulously remunerated. Whatever your experiences with them, there are three ways the chairman can get the best out of advisors for the greater good of the company and shareholders – and you need to get these absolutely right from the outset:

1. **Contact.** You must change the normal contact patterns your advisors have been adopting with the company. It's perfectly natural and right for your advisors to be working with the CEO and executive team on a day-to-day basis. But in a takeover situation the chairman must be directly involved in discussions with those advisors. Have a cup of coffee upfront with the lead advisors and make your expectations crystal clear. A good advisor will know that the client is the company not the management, but they're human too; your expectations should be made clear.
2. **Transparency.** Be completely open with your advisors. If you don't trust them you've got the wrong advisor. If you've got concerns as a chairman about, for instance, dynamics, you must tell the advisors. Otherwise, they can't help.
3. **Incentives.** Think hard about the alignment of your advisors' incentives with what is in the shareholders' interests. The timing and basis of the incentives are important. It's true of management too, of course, but they are normally locked in prior to entering an offer period.

Lawyers aren't such an issue. They are expensive but at least they are on the clock. A seasoned corporate finance lawyer can be a fantastically wise counsel and often go well beyond their legal remit. That's why most of the really good ones often end up as investment bankers. Being focused on your company's risk profile and the risk that the directors are running, they are a sagacious and often under-used commodity.

With investment banks, the natural incentive is biased towards doing a transaction, which can be an issue because you want outcome neutrality. And often, companies are as much (if not more) to blame for this situation. Virile CEOs don't want to pay anything upfront – it's all got to be successful, contingent; but all it does is stack the chips. If you pay for some 'time and effort' money, don't lock in an incentive ratchet until you know the value range and you know what your baseline valuation for your own business is. It's insane to do otherwise.

If you're not in a position where you've got a neutrally-configured outcome, consider an independent valuation from another advisor. You will have to pay a fee for it, but it's quite separate from the actors in your M&A transaction – and it does help keep everybody honest, including the board.

In the end, you must hold the management's feet to the fire. It is the management, not the advisors, who are responsible for outlining 'plan A'. After all, if you keep the company and run it, what value are you going to create as opposed to selling-out? Again, this is down to rigour: have you got a business plan and a clear strategy that you can turn into a valuation? If you haven't, you've got a problem and you will have to move really quickly to get that baseline value.

STAKEHOLDER RELATIONS

In a takeover situation the CEO and chairman are in the driving seat together.In terms of PR and communication, while the CEO should lead the normal public communications, the chairman must be prepared to provide media cover where necessary.

And the chairman certainly needs to be able to speak on behalf of the whole board if it's the board being chastised over its conduct. Indeed, a takeover is one of the few situations where the chairman needs to take a leading role with shareholders. After all, they will want to know that the board is unified around whatever conclusion is being offered.

You certainly need a feel for your bidders and any other counter-parties that are circling, or else you won't know how you judge what's going to happen to the other side and whether they're going to do what they say they're going to do.

Steve Marshall
Chairman
Balfour Beatty plc

Steve was appointed Chairman of Balfour Beatty plc in 2008, having joined the board as a Non-executive director in 2005. He is also a NED of Halma plc, the international engineering group. His former chairmanships include Delta plc, Queens' Moat Houses plc and Torex Retail plc and he is a former NED of Southern Water. Steve is also a former Chief Executive of Railtrack Group plc (now Network Rail).

Contact Steve through www.criticaleye.net