CHAPTER 1

Introduction

The board of directors is responsible for managing, or providing for the management of, the corporation. The directors bring their individual experience and judgment to the boardroom. The board as a whole, or through its committees, provides oversight to the key facets of the corporation’s business over the corporation’s life. Thus, the board selects the CEO, weighs in on major business decisions, and provides oversight to the corporation’s strategy, financial reporting and internal controls, executive compensation, enterprise risk management, and governance. The decision to acquire another company or business can be a significant decision for a company, and the ultimate decision is the sale of the entire company.

Mergers, acquisitions or business combinations (generally, M&A transactions) may not regularly appear on the board agenda, depending on the industry. Of course, we all read about M&A transactions in the daily financial press, and management may regularly consider acquisitions as one way to grow the business, or divestitures as a strategy to focus on core assets. Nevertheless, acquisitions and divestitures are not typical board fare. A particularly acquisitive corporation might have a transactions committee to handle smaller deals, and only the most significant transactions typically come to the board. Many companies do not complete more than one or two significant acquisitions or divestitures over a several-year period.
Moreover, the sale of the entire company is not a regular topic on most board agendas. A company in a consolidating industry may regularly discuss with management and its advisors various strategic alternatives and opportunities for a sale, but the main business of the board is the oversight of the corporation’s strategic business plan, and the main business of the corporation is building stockholder value through the growth of that business.

Thus, while boards often have at least a few directors who have provided oversight for the acquisition or divestiture of businesses or assets, a board may not have any or just a few members who have been through a sale of an entire company. Of course, the sale of the entire company is itself usually a one-time event for the particular corporation (unless the deal doesn’t go through). Thus, a board, although charged with providing oversight to all significant transactions, may not have deep expertise on all of the issues that might arise in a sale of the entire company.

Further, M&A transactions are complex and typically involve a lengthy process; they involve significant decisions about business strategy and deal execution. All of these decisions require board oversight. Indeed, the board is the final decision-maker on whether the proposed transaction is in the best interests of stockholders.

Corporate governance issues—that is, issues for which the board of directors must provide oversight—arise at every step of the M&A process. To start with, how should the board exercise its oversight role and what are its key duties in an M&A transaction? How does the board identify and manage conflicts of interests of directors, management, or major stockholders? What types of advisors will the board require and when? What types of processes should the board implement to consider the M&A transaction? What are the key first decisions to start a sales process, and what should the board consider in making the decision to consider strategic alternatives? What should a sales process look like? What are the board-level issues in the various deal agreements? What happens after signing and before closing—does the board still have a role?

There is a large body of case law governing the corporate governance issues typically arising in M&A transactions in Delaware, where a majority of publicly traded corporations are incorporated. Courts in jurisdictions without well-developed case law regarding M&A transactions will sometimes look to Delaware precedent for guidance, although, as discussed in Chapter 15, there are some states that do not follow Delaware law on particular issues. This Handbook focuses on Delaware law. Delaware courts expect boards to act in the best interests of stockholders, and to be well advised on the issues they confront during the M&A process. This Handbook seeks to
provide an overview to the board of directors and its advisors about the key governance issues in M&A transactions, and the board’s central role in the M&A process.

The Handbook unfolds in three parts. Chapters 2 through 6 set the stage for most M&A transactions, covering the board’s role, conflicts of interest, starting to consider a sale of the company, board process, and engaging the financial advisor. Chapters 7 through 12 cover the key components of the sales process in more detail, including confidentiality agreements and standstills, whether to form a special committee or condition the deal on a majority of the unaffiliated stockholders, the nuts and bolts of a sales process for the sale of control, negotiating deal lockups, and buyers’ issues. Chapters 13 through 16 cover issues that don’t come up in every deal, but require board involvement and good advice: issues relating to Section 203 of the Delaware General Corporation Law, deal derailers (like jumping bidders, stockholder activists, or failures of condition), governance issues in jurisdictions other than Delaware, and private company issues.

By summarizing the key “rules of the road” for establishing good board process for M&A transactions, and by describing the courts’ expectations of the board’s role at key points in the M&A process, this Handbook provides a coherent framework for providing effective oversight of M&A deals. We hope that the Handbook does this in an engaging way, and provides both clarity and good examples for boards and their advisors in pursuing M&A transactions.