An Objective and Diverse Board Can Improve M&A Results

Deal activity has been steadily increasing over the last five years and several factors point to a more robust rebound in 2014. Stock prices have surged, interest rates remain near historic lows; and corporate cash balances and cash flows are at record levels. Given the limited organic opportunities in existing markets, M&A is a crucial growth tool for many companies. However, today's post-recession environment is a cautious one and companies and their boards are sensitive to shareholder concerns regarding the challenges of M&A. As one of the 1,400 directors and business leaders who attended KPMG's Fall Audit Committee Institute noted, "As buyers, we're being more disciplined. We're taking a harder look at the long-term value of a deal, rather than just the one-shot bump in growth that it delivers. Care is higher, even if the dry powder to do the deal is there."

Directors can play an important role in providing discipline to their companies and otherwise improve the M&A process. Indeed, "directors have a unique opportunity to help their companies meet strategic goals through M&A," says KPMG's Tracy Benard. "Frequently, a board will have experienced directors who have worked on many more acquisitions than the management team and will be in a unique position to add value to the M&A process." According to the Institute participants, 23 percent of directors and executives were not satisfied with the value-add the board provides in the M&A process. We believe that boards can help their companies achieve more successful deals in both the M&A process and beyond.

Based on our experience in M&A and interviews with directors who have served on numerous boards, we have uncovered several leading practices that board members can adopt to improve their companies' transactions.

Test strategy alignment and value creation potential

As part of its oversight role, the board should understand the company's strategy, including its organic and strategic growth opportunities, as well as any gaps in talent, technology or products. Boards should monitor whether the company's deal pipeline has the potential to fill those gaps. Generally, deals aligned with long-term strategic goals have higher success rates than more "opportunistic" transactions.

"Another important role for the board is to test the value creation potential of the deal," according to KPMG's Rob Coble. When asked at what point in the M&A process board members could most improve their value-add, both directors and executives across 26 cities overwhelmingly said that they should challenge the value creation potential of the deal (52 percent) and test the alignment of the deal against the company's overall strategy (46 percent). Other important board roles include evaluating and tracking the deal's execution against the post-merger integration plan (24 percent) and assessing whether management has a rigorous M&A process and the right leadership in place (23 percent).[1]

[1] Multiple responses were permitted.

Don't fall in love with the deal

Challenging management's assumptions and limiting some of the enthusiasm for a deal is one of the most important roles the board can play in M&A. To help ensure a more balanced decision making process, board members should focus on the data and analyze the acquisition's value-creation potential, as well as its long-term strategic fit.

"Having access to better data and deeper analysis helps directors ask the right questions," says KPMG's Phil Isom. "It's more important than ever to understand if valuations are consistent with industry norms and if the value creation assumed is realistic for the market."

Closely monitor the due diligence process

"A rigorous due diligence process is an essential element of any successful M&A transaction," says Coble. Institute participants agree and said that the leading causes of M&A failures in their businesses were a lack of rigorous due diligence and a failure to understand cultural risks and roadblocks (32 percent). Another major cause of M&A failure was a lack of accountability for the success of the integration plan (24 percent).[2] As one participant noted, "while the deal is getting done, companies want to save on the costs of due diligence and planning. However, after the deal is completed, that is where you'll get the highest return on your spend."

Examine and track the post-merger integration plan

The board also plays an important role in monitoring the execution of the company's post-merger integration plan, in order to help ensure that the strategic objectives of the deal are achieved. After the deal closes, integration risk and execution risk remain critical areas of focus for the board. "Even with a robust and detailed post-merger integration plan, execution risk can be high, and directors need to focus on execution risk and track performance against the integration plan," says Benard.

Ensure the company has a rigorous M&A process and the right M&A leadership

Boards should make sure that the management team has a disciplined M&A process and employs that process uniformly for every deal. Management's M&A process needs to be rigorous and incorporate a well-thought-out methodology for each phase of the transaction—strategy, valuation, financing, due diligence, synergy identification and capture, closing the deal, and integration.

Companies should have M&A post-mortems and boards should be actively involved in analyzing deal milestones. One important area of focus during the post-mortem is whether key functional areas within the company are comfortable that the concerns they expressed during the due diligence process were appropriately considered.

Boards need to contain diverse roles and perspectives

Having a board with the right composition—a diversity of director backgrounds, perspectives, and skills and experiences—can greatly enhance the board's effectiveness and value-add in the company's M&A process. Directors familiar with the target's industry may have unique insights about the target, while those with more M&A or integration experience can each aid the company during the deal process.

Conclusion

Boards can play an important role in helping their companies capture more value in the M&A process and reduce the risk of failure. Although each transaction presents individual challenges, board members that incorporate leading practices should be able to enhance both the process and the results of M&A at their companies.

[2] Multiple responses were permitted.

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