





BOARD WARS

The fallout from boardroom battles is far-reaching. Public disputes can erode shareholder confidence, cut share prices and damage the company's reputation. They can also put the CFO directly in the firing line.

By Leon Gettler

The public brawl involving Fairfax directors makes an appropriate case study of board wars.

The embarrassing fight erupted when the owners of Fairfax Media's biggest shareholder, Marinya Media – John B. Fairfax and his son, Nicholas Fairfax – said they wouldn't support the re-election of the company chairman, Ron Walker, who had intended to step down in August 2010. After a lot of bad blood and public brawling, Walker finally threw in the towel and said he would not seek re-election at the annual general meeting in November 2009.

The board unanimously selected a former Woolworths chief executive, Roger Corbett, as Walker's replacement. The problem, however, remains unresolved. Marinya Media, which holds a 9.7 per cent stake in the publishing group, had been agitating for an external appointment, suggesting that John B. Fairfax did not regard Corbett as the best candidate.

During the public brawl, John B. Fairfax referred to the way Walker had loaded up the company with debt to make acquisitions. He also referred to its mediocre share price.

When friends fall out

At Perth-based goldminer Troy Resources this year there was a falling out between chairman John Dow and non-executive director John Jones, who also happened to be the company's former chairman.

The pair had gone back a long way, more than 20 years, and had even jointly owned a racehorse. The horse, however, was long retired and put out to stud, and Jones was moving to jettison three of Troy's directors including chief executive Paul Benson and founding director Alan Naylor, and replace them with nominees of his own.

Dow described the falling-out as a clash of personalities. At the time of going to press, Troy's shareholders were scheduled to vote on resolutions to remove the directors at an extraordinary general meeting in November.

Battle at the bank

Another major boardroom dispute was at the National Australia Bank in 2004 when dissident director Cathy Walter, the only woman in the boardroom, took on the other directors after the bank had lost \$360 million in a foreign exchange trading scandal. It was a particularly damaging dispute, which resulted in the departure of the bank's board and management, including chief executive Frank Cicutto and chairman Charles Allen.

The nub of the issue was the NAB appointing PricewaterhouseCoopers to investigate the irregular trading of foreign currency options. Walter, who had headed the audit committee, raised concerns about the independence of that report in light of the close and extensive relationship between NAB and PwC. In the end, Walter stepped aside but the boardroom battle shook the NAB to its foundations. The bank was forced to examine its culture and then do its best to change that culture.



As a study in board wars, that reference to debt and share price is significant. One of the key reasons why boards break down comes down to money. John B. Fairfax's fortune has slumped sharply with the fall in the media company's share price.

Finance is the trigger

Gess Rambaldi, the partner in charge of the business recovery and insolvency services division of Pitcher Partners, says finance is often the trigger for board wars. He says boards are now more vulnerable to civil war because of the economic climate. Losses and low-level profits in the aftermath of the economic downturn will exacerbate boardroom disputes.

"When the economy starts to turn around, you do start to see more boardroom disputes because things are tough. When things are good, people tend to gloss over differences; when things get tough they start to dig their heels in and friendship sometimes goes out the window," he says.

"And in a time such as the present, when you have more financial distress than perhaps is normally the case, you do tend to see more boardroom disputes occurring."

Personal differences

Of course, there are other reasons too. Directors, for example, might disagree about the vision some of their colleagues. Or, as Rambaldi says, it might just come down to personalities. "There is no law that says directors need to get on, and sometimes they simply don't," he says. An example of this came at Perth-based goldminer Troy Resources this year (see box, left).

Smaller companies vulnerable

Corporate governance specialists say small cap companies, such as Troy Resources, are more vulnerable to boardroom disputes. One reason for that is certain shareholders, including directors, can take out big blocking stakes. It is worth noting that chairman John Dow owns 13.3 per cent of Troy Resources.

Ian Ramsay, director of the Centre for Corporate Law and Securities Regulation at the University of Melbourne, says the dynamics in small caps make boardroom disputes more likely. "Often, they are a big shareholder and quite often they're involved

in management, so they have more at stake. That more frequently leads to boardroom wars," Professor Ramsay says.

"We also see that in litigation. There is much more litigation concerning boards in the small company sector. That seems to be part of the rationale that more is at stake

"In the big listed sector, you might be a non-executive director and have a trivial shareholding but in the smaller sector it's quite common for significant shareholders to be on the board, to be involved in management in some way, so it's not easy to let go if there is a dispute."

Keeping the corporate ship steady

Ramsay says there is another very good reason why boardroom battles tend not to erupt in large companies – Australia's biggest corporations are controlled by institutional investors that have a vested interest in keeping the ship running. "They effectively control voting for the major corporates and as a general rule, they are not interested in participating in brawls," he says.

Or as Dean Paatsch, head of corporate governance advice group RiskMetrics Australia, says, large corporations are more stable and that's just self-fulfilling. "It tends to happen in the smaller cap companies much more than the larger companies and that's a self selection thing," Paatsch says. "You don't get to become a big-cap company if you've got an unstable shareholder base or an unstable board."

Disputes cost dearly

That said, large corporations are not immune to boardroom disputes. Fairfax is only one example. In 2002, Solomon Lew was voted off the board of Coles Myer. Lew had served as an executive chair of the retailer.

The chairman of the company, former banker Stan Wallis, had campaigned for Lew's removal, lobbying insurance companies and banks and other major institutional investors. Lew's removal followed the Yannon scandal, an affair that shook Australia's biggest retailer when it came to light in 1995.

At the time, the company's finance director, Phillip Bowman, raised questions of impropriety. In that scandal, an undisclosed indemnity was given by Coles

Myer to a shelf company called Yannon, set up by CS First Boston. It bought shares in a company called Premier, a major shareholder in Coles Myer controlled by Lew. It guaranteed Yannon against any losses in the share deal. That eventually cost the retailer \$18 million. It retrieved \$12 million in a later agreement between itself, Mr Lew and with other parties.

Operations under threat

Boardroom wars can have also a devastating impact on company operations. To begin, it would affect its ability raise capital. Paatsch says: "If someone was attacking the company, I don't think your lenders would be looking at that and saying fantastic. You would think that any major leak or destabilisation would have a major impact on your ability to raise finance or corporate capability."

As Ramsay says, operations are set adrift when there is a dispute. "If you have got a boardroom brawl, by definition it looks to be a dysfunctional board. It's either dysfunctional or a board whose eye is off the main game, engaging in the dispute at the expense of time devoted to the operations of the company. Under either alternative, it's a losing situation for shareholders."

CFO in the firing line

Disputes can also leave staff and professional advisers in a no-win position. Rambaldi says it can become particularly difficult for senior managers, including chief financial officers. If the dispute is around finances, or vision and direction, they might well be dragged into the dispute. And that could damage their reputations, and leave them in potential breach of the law.

"The CFO will find, for example, that he has to repeat everything to different people," Rambaldi says. "In a normal situation, you might have a line of authority and report to one particular person and you obtain directions and authorisations from that person.

"Where you have conflicts, that person's authority has been undermined and in order for you to achieve your role, you might find you might have to seek approval not just from one line of authority but different lines, so you are having to repeat yourself a number of times."

It is also fraught territory for professional advisers such as accountants. They need to ensure their advice is in the interests of the company. The advice may not necessarily be the interests of the director but then, advisers need to remember that their client is the company. That can be difficult where there are close and longstanding relationships.

"The accountant is caught up in the whole thing because he has personal relations with directors. But he has to remember that when directors are fighting amongst

[The accountant] has to remember that when directors are fighting amongst themselves, his client is in fact the company, not a director or directors.

themselves, his client is in fact the company, not a director or directors.

"It is very easy to be drawn into taking sides or seen to be taking sides with a director. But in those circumstances you can be not only losing a client but your reputation can be damaged in that process."

Potential breach of directors' duties

More to the point, it can leave the adviser exposed legally. The Corporations Act requires directors to serve the interests of the company.

Under Section 79 of the Act, there is a contravention if someone "has aided, abetted, counselled or procured the contravention ... in any way, by act or omission, directly or indirectly" or has "conspired with others to effect the contravention".

"If you are a professional adviser to a company and you find directors are fighting, you might find that one director might be acting in his own interests rather than the interests of the company," Rambaldi says.

"To that extent, the director is in breach of his duties. If you are assisting the director rather than the company, then you as a professional adviser might find yourself in trouble by virtue of the Corporations Act."

Damage limitation

Still, boardroom disputes are inevitable. Different personalities have different perspectives, and finance will remain a trigger point. The problems may well be exacerbated in this market. However, managers and professional advisers can take steps to minimise, or even defuse potential blowouts.

Keeping everything documented and backed up is critical, says Rambaldi.

"First and foremost, you have to recognise who the client is to and keep accurate

records of discussions between yourself and the directors," he says. "As a professional adviser you have to ensure you are always giving advice, not instructions. Give them options and advise them of pluses and minuses. Give them options and let them make up their mind."

He says planning ahead is important. Drawing up plans in the early stages of the company, covering strategies around potential disputes and containing exit clauses would be particularly beneficial. Smart companies will plan ahead before the dispute happens.

"These documents, if properly thought through, provide mechanisms to defuse or avoid disputes between the owners of the business," Rambaldi says.

"It works exceptionally well if it's included as a 'pre-nup'. It can be done during the business evolution but it works exceptionally well if it's done at the beginning.

"And sometimes it might be better to bring in an external party to act as mediator." ▀



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