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Can Willis-Towers Merger Pass With Proxy Advisors' Opposition?

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A few months ago, American chemical giant DuPont defeated Trian Partners in a proxy fight to replace four directors even though the major proxy advisors (ISS and Glass Lewis) supported the activist. Over the next week, we will be watching to see whether the $18 billion merger of equals between global professional services provider Towers Watson and multi-national insurance broker Willis Group will be approved when the proxy advisors are again aligned with an activist.

On June 30, 2015, the merger was announced with terms that would have Willis shareholders owning 50.1% of the combined entity upon closing. Towers shareholders would receive Willis shares based on an exchange ratio and a one-time special cash dividend of $4.87 per share which, in effect, asks Towers shareholders to accept a 9% discount to the closing price prior to the announcement.

On September 15, 2015, Driehaus Capital Management, a 1.5% holder of Towers, filed for exempt solicitation and published a white paper opposing the transaction citing the inadequate "take-under" offer price and questionable synergies. ISS also was not convinced by the primary thesis of a Willis-Towers merger, i.e., a stronger joint entity enabling cost-synergies driven by tax savings, the diversification of Willis beyond insurance and reinsurance brokering, and the expansion of Towers' exchange business through Willis' distribution network, and did not recommend that Towers' shareholders vote in favor of the transaction. In a research report issued on November 5, ISS stated that "the magnitude of the discount [Towers shareholders] are being asked to accept appears excessive given Towers' standalone outlook and its strategic contribution to the combined entity". However, in a separate report for Willis shareholders, ISS recommended they support the transaction. Glass Lewis also recommended that Willis shareholders support the deal but Towers shareholders vote against it. With both proxy advisors recommending against the transaction at the Towers meeting, one would question whether this was merely another kink to iron out or the nail in the coffin for the prospects of a Willis Towers Watson.

In the case of DuPont last May, while both ISS and Glass Lewis recommended on the dissident proxy card and in favor of some of Trian's nominees, none of the dissident directors was able to secure a board seat. One can reasonably conclude that a majority of voting shareholders made up their own mind about who was better suited to run the company. For institutional investors, the recommendations of proxy advisors, while likely respected and possibly acknowledged, are rarely ever worshipped – in contested situations and high-profile transactions, these shareholders vote on a case-by-case basis. Since retail shareholders held in excess of 30% of DuPont shares, management made it a priority to target the retail votes and also to continue their regular engagement with institutional shareholders leading to their ultimate success. But success is less defined in the world of contested meetings. On the surface, Trian's objectives were defeated with the board's successful blockade of any board membership from Peltz and party. However, looking back at the two year period since Trian unveiled its plan for shareholder maximization, a $5 billion share buyback program was announced and the Performance Chemicals segment was also spun off.

Surely, onlookers are hard-pressed to not credit Trian with at least some of these achievements. To further muddy the waters, months after the conclusion of its proxy contest, DuPont announced in early October 2015 that Ellen Kullman, the CEO who led DuPont through the recent proxy contest, was stepping down from the helm of the company. She was succeeded by Edward Breen, one of the two “superstar” directors recruited amidst the fight. Breen was given the Chairman and CEO title after serving as the interim CEO for only a month, during which period DuPont’s stock outperformed the Dow Jones Industrial Average significantly to recover most of the loss earlier in the year.

Unlike DuPont, Towers has relatively little retail ownership and thus the institutional vote will prove to be that much more significant. Undeterred by the power of proxy advisors and in a rare public intervention, another activist, ValueAct, issued an open letter on November 10, 2015 to Towers shareholders, criticizing ISS for focusing on the short-term gain of the transaction and ignoring long-term benefits. “The behavior that ISS is legitimizing actually has a name among M&A professionals, ‘bumpitrage’,” the letter says. “This is one of the most short-term flavors of stockholder activism, particularly in situations where the stockholder activists purchase the target company stock exclusively to lobby for the proverbial bump.” Of course, one should note ValueAct owns 10.2% of Willis but less than 1% of Towers. ValueAct also has a voting agreement to support the transaction at Willis’ shareholder meeting.

Towers and Willis shareholders will cast their votes for the transaction at their respective meetings on November 18. While it is unclear as to how the transaction will play out, we are interested in seeing how shareholders vote in the face of negative proxy advisor recommendations and ValueAct’s latest endeavours to dismiss ISS , whether or not a ‘take-under’ of this sort can be achieved without advisory approval and, if not, whether further developments will unfold.

If you have any questions about this update, please feel free to contact Victor Li or Jackie Cheung directly to discuss.

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