

**EMERA'S TAKEOVER OF LIGHT & POWER  
HOLDINGS LTD: A CASE STUDY IN  
CORPORATE GOVERNANCE AND TAKEOVERS  
IN THE CARIBBEAN**

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# Motivation for Study

- Importance of Light & Power Holdings Ltd. (LPH) to Barbados
- Takeover scenario presents a unique opportunity to evaluate corporate governance
- Corporate governance topical in finance due to spectacular implosions of large companies (Enron , CLICO, Olympus)

# Barbados Light & Power: History

- 1899 - the passage of the Electric Light & Power Act by the Barbados House of Assembly
- 1909 - Barbados Electric Supply Corporation (BESC), the predecessor of Light & Power Holdings, was founded
- 1930's – Period of social unrest
  - Subsequent redress to social and economic inequality accelerated adoption of electrical service across social spectrum

# Barbados Light & Power: History

- 1966 - Growth in customer demand forces LPH to acquire a 5.5 acre site to expand operations.
- 1970 – In the 4 years following the expansion, customer base grows by 10,000 representing a staggering 33% growth in customers

# Barbadians: Stakeholders In Barbados Light & Power Ltd.

- 1970 – Local shareholders numbered 1,300
- 1980 – 52% local ownership
- 1983 – Number of local shareholders increased to 2,265
- 1997 – Shareholders form a parent company, Light & Power Holdings Ltd.
  - 63% locally owned
  - Approximately 2,800 Barbadian investors
  - Intention to diversify holdings
- Remaining shares owned by American company Leucadia (37%)

# Barbados Light & Power: Financial Performance

Year	Revenues (\$Bds 000's)	Net Profit (\$Bds 000's)	Dividends/Share (\$Bds)	Total Dividends Paid (\$Bds 000's)
2002	<b>241,904</b>	<b>15,308</b>	.40	5,357
2003	<b>272,490</b>	<b>10,736</b>	.40	5,800
2004	<b>301,593</b>	<b>26,816</b>	.40	5,811
2005	<b>339,231</b>	<b>15,389</b>	.40	5,818
2006	<b>361,653</b>	<b>30,366</b>	.40	6,119
2007	<b>397,636</b>	<b>58,350</b>	.40	7,001
2008	<b>473,310</b>	<b>31,716</b>	.40	6,856
2009	<b>415,392</b>	<b>27,455</b>	.40	6,872
2010	<b>508,139</b>	<b>45,646</b>	.40	6,865

# Barbados Light & Power: Demand Growth

Year	Peak Demand (Megawatts)	Sales (GWh's)	Domestic Customers	Commercial Customers
2001	<b>130.4</b>	<b>735.0</b>	90,194	12,938
2002	<b>134.7</b>	<b>763.9</b>	91,641	13,554
2003	<b>141.6</b>	<b>805.9</b>	92,809	14,423
2004	<b>143.0</b>	<b>831.3</b>	94,045	15,443
2005	<b>154.2</b>	<b>992.8</b>	95,223	16,520
2006	<b>157.0</b>	<b>1,020.4</b>	96,486	17,775
2007	<b>162.4</b>	<b>1,049.2</b>	97,801	18,857
2008	<b>164.0</b>	<b>1,053.7</b>	99,000	19,798
2009	<b>165.7</b>	<b>1,068.4</b>	99,748	20,874
2010	<b>167.5</b>	<b>1,078.3</b>	102,407	19,699

# Light & Power Holdings: Source Of Competitive Advantage

- LPH positions Barbados to better compete for foreign direct investment.
- **The Global Competitiveness Report 2009-2010** rated Barbados 24<sup>th</sup> worldwide with respect to the quality of electricity transmission.
  - Ranked above countries considered more developed such as Ireland and Australia



# Light & Power Holdings: Takeover Scenario

- **Jan 2010** – Fair Trading Commission granted LPH a guaranteed rate of return of 10%, up from 6.7%.
- **May 2010** – Emera became largest shareholder after buying Leucadia's shares
- **Dec 2010** – Emera tendered an offer for any and all outstanding shares (i.e.) takeover bid
- **Jan 2011** – End of the offer period. Emera now owns roughly 80% of LPH – successful takeover

# LITERATURE REVIEW

# Corporate Governance Concepts

- Central concept is that of agency costs caused by the separation of ownership and control (Berle & Means 1932)
- Jensen & Meckling (1976) define agency costs as monitoring costs by principals, bonding costs by agents, **residual loss due to their divergent interests**
- Tirole (2006) attributes agency costs to insufficient effort, extravagant investments, entrenchment and self-dealing

# Corporate Governance Concepts

- Hart (1995) reframed corporate governance as mechanisms that manage control residual to contracts between principals and agents.
- Stakeholder view of corporate governance which considers the interests of all a firm's stakeholders, not just those of its shareholders. (Freeman 1984).

# Making It Work – Key Mechanisms

- **Board Of Directors**

- Characteristics:

- Size (larger boards are inefficient but may be better at restricting opportunistic management)
    - Stakeholders represented and to what extent
    - CEO-Chairman duality thought to undermine governance

- Whether or not the board is “captured” by management

# Making It Work – Key Mechanisms

- **Large Shareholders**

- More likely to monitor the firm's management and have to have greater influence on management's behaviour
- This should result in better performance in the interest of all shareholders
- Not always the case since the interests of large and small shareholders do not necessarily coincide

# Making It Work – Key Mechanisms

- **Takeovers**

- Market monitors for signs of underperformance and may take over firms with unfulfilled potential
- Signalled through the firm's share price
- Managers focus on maximising firm performance to avoid takeovers
- Results in fixation on share price

# Characteristics of Caribbean Corporate Governance

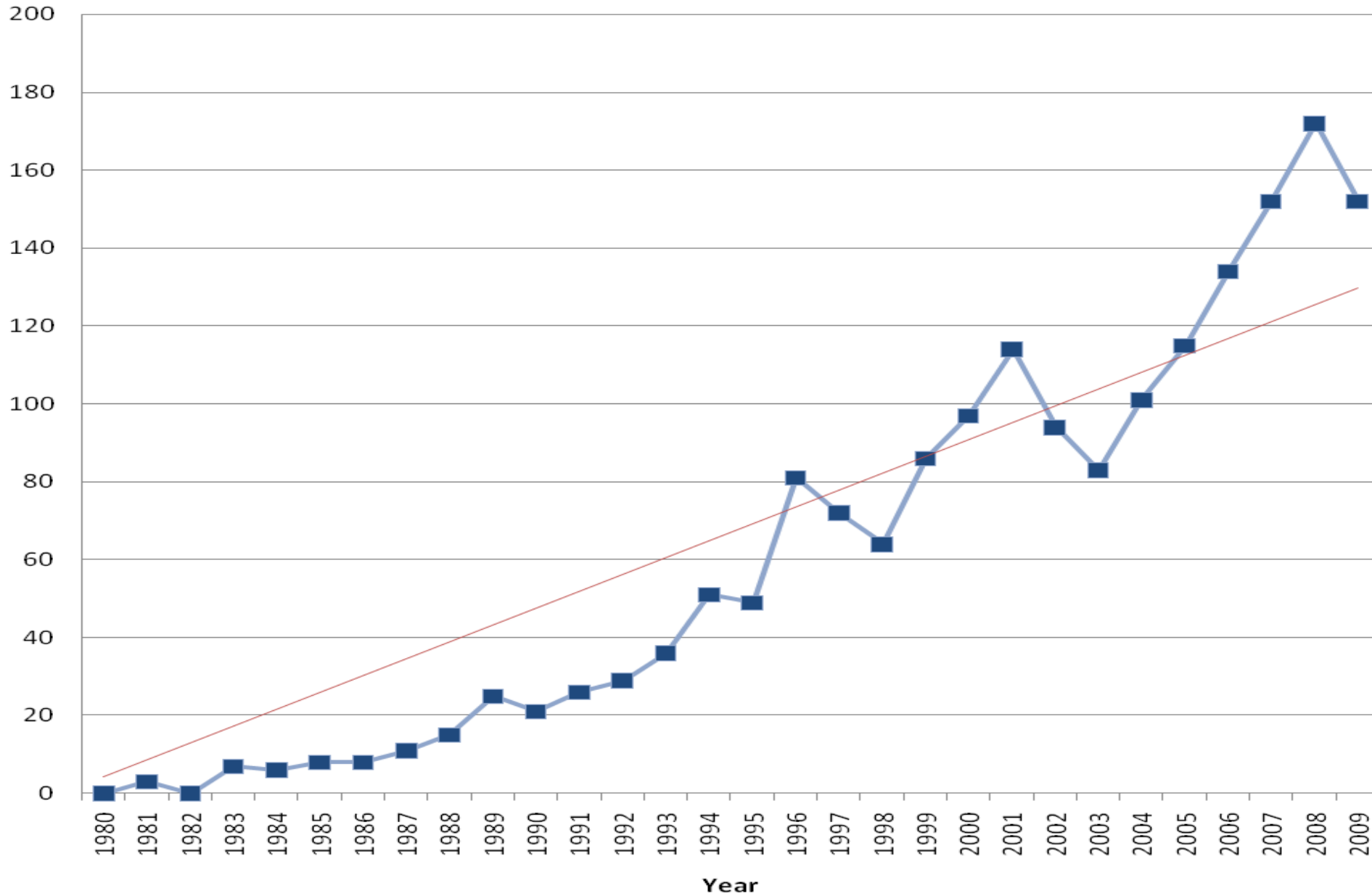
- Issues with influence of large shareholders (Kerr 2007)
- Board characteristics following international trends to improve governance (Kerr 2004)
  - Smaller boards
  - Infrequent CEO-Chairman duality
  - Higher proportion of non-executive directors



# Characteristics Of Takeovers in the Caribbean

- Trend of increasing takeover activity
- Hints that the increase is driven by foreign companies acquiring domestic ones

Number of Takeover Deals in the Caribbean  
1980 - 2009



# **DISCUSSION AND ANALYSIS**

# Corporate Governance - The LPH Case

- Strong case for adherence to stakeholder view of corporate governance.
  - Government compelled to establish a fund to assist those struggling with electricity prices
  - Reduced demand in 2011, first time in 37 years
  - Strategy to diversify energy sources benefits shareholders and other stakeholders

# Corporate Governance - The LPH Case

- Threat of takeover not a viable mechanism to induce managerial effort (prevent agency costs)
  - Share price virtually unmoved on announcement of guaranteed rate-of-return increase or change in largest shareholder from Leucadia to Emera
  - No incentive for managers to expend additional effort since changes in LPH's prospects are not reflected by changes in its share price

# Corporate Governance - The LPH Case

- Concerns about characteristics of LPH board
  - Board size reduced **but**
  - Net reduction in non-executive membership
  - No CEO-Chairman duality **but**
  - Chairman – Largest shareholder duality

# Corporate Governance - The LPH Case

- Board's fulfilled its mandate to shareholders when handling Emera's takeover bid:
  - Board advised shareholders of bid and suggested they not sell unless the fairness of the offer was assessed
  - Commissioned independent assessment of the fairness of Emera's offer
  - Bid price was found to be fair by assessor despite difference between bid price (\$25.70) and the assessor's valuation (\$33) (market price was only \$12)
  - Board was obligated to inform shareholders of the fairness and advise accordingly (sell!)

# Takeovers- The LPH Case



- Takeover scenario reinforces concerns about influence of large shareholders.
  - Telltale consequences of a takeover include change in board structure, company strategy, company management
  - Did not occur after successful bid but months earlier when Emera became largest shareholder
  - Becoming largest shareholder = De facto takeover?
  - Then why embark on takeover? Evidence suggests Barbados's double taxation treaty with Canada.



# Takeovers- The LPH Case

- Takeover was corrective in that LPH's change in strategy recouped losses LPH's previous diversification strategy.
- Takeover continues trend of foreign firms acquiring domestic firms

# Corporate Governance-Takeover Relationship In The Caribbean

How:	Influence(s)	Corporate Governance	Takeovers
Corporate Governance		<i>Not Applicable</i>	<i>Achieving a large shareholding is tantamount to a staging successful takeover due to the Caribbean corporate governance environment.</i>
Takeovers		<i>Takeovers can be corrective corporate governance mechanisms, but not preventative ones.</i>	<i>Not Applicable</i>

# Implications Meriting Further Exploration

- Asymmetries in information and monitoring costs may predispose smaller shareholders to sell to larger shareholders, making it easier for large shareholders to effect takeovers.
- Illiquid Caribbean stock markets may subject public companies to predation as a consequence of systemic under-pricing.
- The Caribbean corporate governance environment may allow firms to be “acquired” at a discount by affording excessive control to large shareholders.

# CONCLUSION

# Conclusion

- There is a relationship between corporate governance and takeovers in the Caribbean.
- Takeovers not an effective preventative Corporate Governance mechanism in the Caribbean as suggested in the literature but can act as an corrective corporate governance mechanism.
- Scope for investigating determinants of increased takeover activity.
- Study accords with previous findings that the power afforded to large shareholders in the Caribbean may undermine corporate governance
- Stakeholder paradigm of corporate governance is particularly important in the light of increasing foreign takeovers.

# Comments & Questions