

CHAPTER NINE

SHAKING UP THE CORPORATION

TransAlta and Crestar Energy

FERNANDO FLORES IS THE FORMER economics and finance minister of Salvador Allende's ill-fated government in Chile. He was imprisoned for three years by Allende's successor, the military dictator General Augusto Pinochet. After his release, Flores took a PhD in philosophy at Stanford University and started four companies in California, one of them called Business Design Associates. BDA supposedly builds on his revelation in prison, where he endured mock trials and solitary confinement, that "communication, truth, and trust are at the heart of power." Translating that idea into the corporate world, often charging \$1 million or more for his services, Flores used verbal shock tactics to change the behaviour in an organization. One of the companies BDA tried to transform was TransAlta Corporation, where I went on the board in 1991, at the end of my time with Interhome, and then became chairman five years later. In 1992, the first of Flores's people arrived at TransAlta to work on about thirty different training programs. His style then was to confront employees and managers over their weaknesses—sometimes calling them "assholes" or worse—and to push them into voicing strong and often highly critical assessments of their colleagues. In TransAlta's case, his methods backfired badly.

TransAlta's roots go back to 1911 and Calgary Power, Alberta's first large-scale electric-energy company, which harnessed hydro

power generated on the Bow River. Its base was in Montreal, and its founding president was the Canadian business tycoon Max Aitken (who was later owner of a major newspaper chain and a cabinet minister in England, where he was knighted as Lord Beaverbrook). In 1947, the year of the Leduc gusher, Calgary Power finally relocated its head office to the city it was named for. By then, it was supplying 99 percent of the province's power and soon turned to thermal generating plants fuelled by coal and natural gas. A decade before I became a director, it became TransAlta and was well on its way to being Canada's largest private power producer in a capital-intensive industry.

There was a long-standing invitation for me to join TransAlta's board. I was a friend of both Marshall Williams, who had been the well-respected chairman of Calgary Power, and TransAlta's current chief financial officer, Harry Schaefer, who had done Arthur Andersen audits with me during our articling days. So in 1991, as I was deciding to play more of a director's than a CEO's role in future, the company seemed an attractive place to be.

As a regulated business that had been in a near-monopoly position for decades, it had a good rate of return on investment, a high dividend payout, a nice cash flow, a strong balance sheet, and one of the very best credit ratings. But for all its apparent achievements, the company began to have problems. It had tried, and failed, to get into the oil business, for instance, and its expensive strategic alliance with a local software company that was developing a communications link among various word-processing programs seemed to be like tossing money down a dry hole.

By 1993, earnings of \$169 million were down slightly, and the following year, as the executive team feared the rise of independent power producers, it cut 350 employees in the first-ever wave of layoffs. The remaining staff was placed on notice. As Ken McCready, the current president, put it, they were "polite and friendly people who would listen to customers, agree with them, and then go away and do their own thing." The sledgehammer solution to reverse this attitude was to call in Flores's Business Design Associates and use techniques that were originally developed and paid for

by Werner Erhard, the founder of the controversial, cult-like EST (Erhard Seminar Training) movement.

Ken himself was part of the problem. There's no question that he was a forward-thinking leader who pioneered co-generation projects that use power stations to generate both heat and electricity at the same time. An electrical engineer, he'd been with the company since 1963, becoming president in 1985 and then CEO only two years before I came on the board. The senior role, which paid him about \$1.5 million a year, seemed to go to his head as he became a director of other companies and spent too much time outside TransAlta on causes like sustainable development (which has been defined as any kind of development that meets the needs of the present without compromising the ability of future generations to meet their own needs). Meanwhile, the economics of the co-gen plants didn't appear sound enough, initially. In one case, our directors took exception because Ken didn't even have the figures on hand to justify a project because he was too busy doing other things. He was losing the confidence of the board.

Harry Schaefer, the chief financial officer, explains Ken's style: "He would have lots of projects and people studying them and was not quite sure which were the right ones to do. Then time would run out, and he would just pick one—as opposed to a true leader, who picks out the direction you should be taking and shapes it. In the end, he turned to an outsider to get the sense of direction for the company."

One of Ken's most questionable decisions was to bring in Fernando Flores and BDA. Their deal was to get a share of any savings from cost reductions that they produced. But an old established company like TransAlta should have tried to make the bulk of those cuts first and *then* called in experts to trim the final 10 percent or so. Worst of all, BDA's tactics appeared as bullying to many of our 2,100 employees, causing them to burst into tears, to attack one another, or even to resign in shame and disgust. One employee who quit later told the *Financial Post*, "They want people to be blunt and not spare another person's feelings. I felt emotionally abused when this was brought into the day-to-day

work environment.” Another sent an anonymous letter to TransAlta’s regulator, the Alberta Public Utilities Board, complaining that the staff had been “subjected to humiliation and psychoanalytic sessions”—like a form of brainwashing.

TransAlta had another problem that needed fixing: Harry and Ken McCready had risen through the company together, and when Marshall Williams retired as chairman, the directors tried to be fair to the two competitors who were bidding for the top positions. So they appointed Harry chair and Ken chief executive officer. Now Harry was both the CFO reporting to the CEO as well as the chair supposedly overseeing the CEO. What an unworkable situation.

Just before the problems with the BDA consultants reached the media, Harry and Ken asked for a luncheon meeting with me and another director, Ross Phillips, the former Home Oil president. We were told that an American television program was about to report on Fernando Flores and his controversial projects, including the one at TransAlta. And then I saw a local TV show that contained footage of our employees being berated and crying in front of their peers. I was so damn mad because nobody within the company had previously informed me or the other board members that this totally unacceptable behaviour had been happening under our noses. It was embarrassing that in the relatively small business community of Calgary, we hadn’t heard about this mess.

I was furious, and my anger was multiplied by the fact that some well-placed rivals in the industry *had* known. After the situation became public, I was flying back from a Hawaiian holiday with Ron Southern and his wife, Margaret, who confided in me, “Dick, I feel badly now that we didn’t tell you what was going on. I can’t believe that you wouldn’t have known. We didn’t want to tell you because we were competitors [with ATCO’s Canadian Utilities] and it would sound like we were bad-mouthing TransAlta.”

Ken had commissioned a study by Stephen Murgatroyd, who ran the Centre for Innovative Management at Athabasca University, the distance-learning institution in Edmonton. Reporting in December 1994, Murgatroyd said, in the jargon of his trade,

there was a “disconnect between [the] top, middle and bottom of the organization” and “between personal transformation and organizational transformation in the minds of many employees.” As a result, the company “needs to be concerned that some able, talented and dedicated staff who are producing value are beginning to look to their future outside of TransAlta and are looking at TransAlta as a place where the promise may not be matched by performance.” In other words, a fine mess.

In January 1995, Ken McCready announced that staff no longer had to take Fernando Flores’s training—though in a face-saving move, he said it was still available for those who wanted it. The following November, the corporate board set up a special committee to delve into the continuing morale problems. Heading it was Gerry Maier, a director for more than a decade, and its two members were me and Charles (Chuck) Hantho, our strong chair of corporate governance, who used to run C.I.L. Inc. Our mandate included analyzing McCready’s capability to lead the company into the coming deregulation of the Alberta utilities industry and also considering his potential successors. We brought in my semi-retired colleague Ken McNeill, with his sterling human resources background, as an advisor reporting only to us. His contract ended with the caution: “Time is of the essence.”

In no time at all—January 1996—Gerry and I told McCready, “Ken, it’s all over.” The board found an interim president and CEO for TransAlta Corp. in Walter Saponja, a salt-of-the-earth engineer who was the highly efficient president and chief operating officer of its subsidiary, TransAlta Utilities. I’d become non-executive chairman of the parent company, replacing Harry Schaefer—but only after Ted Newall checked with the OVA board whether any of its directors saw a conflict in my accepting the TransAlta position. One of them former Scotiabank chair Ced Ritchie, immediately called me to say, “This is an important company in your part of the world, and it’s your civic duty to accept it.”

My first major task, along with a search committee of directors, was to find a permanent CEO, someone who could shepherd us through deregulation, when any new facilities would have to

compete in a free and open provincial marketplace. We found two terrific candidates—neither of them with any experience in the utility industry. One was running a Canadian agricultural products giant. The other was Steve Snyder, who had a superb track record as an entrepreneurial leader focused on business development and marketing—two key areas that would shape TransAlta’s future. His most recent position was president and CEO of Noma Industries, which Canadians knew as the Christmas-lights company. But we were most interested in Steve’s role as chairman and CEO of GE Canada, the domestic subsidiary of the global General Electric Corp. colossus.

Steve was a youthful-looking forty-seven-year-old with rapid-fire speech and hands and arms that were endlessly in motion—an aggressive yet personable guy. The son of a clothing store manager, he called himself “the classic Canadian—born in Montreal, went to public school in Alberta (Edmonton and Jasper), high school in Montreal, university in Ontario.” Steve took a chemical-engineering degree at Queen’s and then, after a year with marketing-oriented Colgate-Palmolive, felt in need of an MBA, which he got from the University of Western Ontario. He went to work for GSW Inc., the sole Canadian-owned, full-line appliance company, streamlining the shipping of products to cut costs. The privately run GSW merged with GE Canada to create a joint venture called Cameo, which bought the Canadian major-appliance division of Westinghouse. That launched Steve’s fourteen-year career with GE. He was vice-president and general manager of GE Lighting and marketing VP and, eventually, president and CEO of Cameo, which was then a public company doing about \$600 million in business. The two partners in Cameo had an antagonistic relationship, which Steve found challenging but fun to mediate.

In 1989, a few weeks after he’d become chief executive, his wife died, leaving him with an adolescent son and daughter. Two years later, GE offered him the managing director’s post at Eurolec PLC, its appliance company based in Brussels. After quickly realizing that all the European travel was alienating him from his children, he returned to Canada as chair and CEO of GE Canada.

But because the parent company had him on a promotion track that demanded international transfers, he left in 1992 to join Toronto-based Noma Industries. A family enterprise Noma had its own challenges. Steve was the first non-family executive, aside from a president who'd been with the business for half a century. It expanded from a Canadian consumer-products manufacturer to a maker and distributor of industrial products such as auto parts. In 1995, Noma earned more than \$13 million after losses during the previous five years. A year later, when the founders' daughter was being primed for the presidency, Steve decided to skedaddle.

After an Alberta friend tipped him off to the opening at TransAlta, he exercised due diligence by doing some research about the changing nature of the utility industry. He asked the headhunters to put his name in the hat—only to find out that he was already on their list. Gerry, I, and others on the search committee liked his experience with GE, which under Jack Welch had popularized many effective techniques of human resource development during the 1990s. Among them was the idea of offering people jobs in various areas early in their career—“Let them learn from their mistakes at a time when the damage is controllable,” as Steve expressed it. “If you wait for twenty years to put them in a key job and they fail, it's cost them and the company big time.”

What we sensed—and proved true—were his strong communications skills. His first challenge was dealing with the scars from the BDA mess, still smarting after a year. He made sure he went to every plant and met every junior employee in the office. And he held back from letting any unproductive senior people go for several months until he had a good fix on their abilities. Dealing with his directors, he worked hard at informing us with regular written updates and bringing his management team in front of the board to present a unified front and explain their collective decisions. As Steve said, “I'd rather make my stupid decisions with the board in the boardroom than in public.” I tried to facilitate those appearances by putting myself in the managers' shoes, attempting to understand the logic behind their actions, and helping to translate their thought processes to my colleagues.

Steve appreciated the fact that I was a non-exec chair, which was still a rare animal in Canada. “A lot of people don’t understand how different that role is than just chairman,” he says. “A non-executive chairman is one of the most challenging roles because most of the people in those jobs have run companies—and when you’re in that chair, you’re not running anything. You are managing board dynamics and laying out a course of action. What a non-exec chair needs to do is set the tonality, help set the agenda, and engage the board and management in discussion. Create an atmosphere where the directors and managers can have a discussion together—as opposed to presentations by management, which the board then critiques, and those who yell the most get the attention of the board. Communicate to a CEO what the board issues are without telling him what to do about it. Translate concerns back to the board in a way that they understand where the CEO is coming from.”

Some of the decisions Steve made in his first two years were momentous. Running out of growth opportunities in Canada, TransAlta had been expanding internationally under Ken McCready, but not always wisely. Steve explains the situation: “The theory was, I think, to spread risk. But my view was that they ended up with three countries that were successful, three that were awful—and the net effect was zero. We had people doing projects where there was no hope in heck we were ever going to succeed, yet we were tying up people and resources. I had customers in Brazil saying, ‘When are you going to do this project?’ I said, ‘I don’t think we ever will.’ ‘Well, why is your guy down here talking to us, then?’

“And the other thing was that the company was making about a 10 percent return and told the board it could make 15 percent by going international. Problem was, you really needed to make 30 percent for the risk you were taking in these countries. Argentina was a disaster, and we wrote off \$100 million in hydro facilities there. Then the board specifically said, ‘Look, we’ve got this little thing going on in New Zealand, we’re not sure what it is.’ So I went down to New Zealand, and my conclusion was this

thing actually has some legs to it, this may be the one we should keep. We were very small then, just building one plant. But we did a couple of acquisitions and became effectively the largest retailer of electricity in New Zealand.” Later, when the nation changed governments and decided to close the market, TransAlta sold at a peak price to locals who did poorly with the operation. The company went on to acquire and sell electricity generation and transmission resources in Western Australia while keeping a few small plants that, on a per-megawatt basis, became its best performers.

By then, I had resigned as chairman. Under deregulation, TransAlta and TransCanada Corp., where I’d also been appointed chair in 1998, would become head-to-head rivals. TransAlta asked me to stay on as a director, but after a couple of meetings where I had to excuse myself as competitive projects were being discussed, I decided to go with TransCanada .

For a time afterwards, TransAlta was stumbling. Utilities get bored doing their basic job, so they often look for bigger markets and ventures with potentially higher returns. My friend Tom d’Aquino of the Canadian Council of Chief Executives quoted Steve in *Northern Edge: How Canadians Can Triumph in the Global Economy*, a book he wrote with David Stewart-Patterson:

The big challenge for us is growth. Provincial regulations make east-west growth extremely difficult. We’re already large in our home province. We were forced to go international, but with at least one arm, if not our legs, tied behind our back.

Steve and his people bought the sizable Big Hanaford coal-fired plant in Washington and (as TransCanada did) got involved in trading power in the U.S.—all of which lost money. After I sold most of my shares in the mid-to-high 20s, the stock kept falling, along with the corporate credit rating, though shareholder still got a dividend annually. At one point, TransCanada considered taking the company over on a friendly basis. The two seemed to

be a natural fit, but then TransAlta got back on track. It had to decide whether it could continue investing in both the generation and transmission of energy and whether it should remain in the distribution and retail (D&R) business. In 2002 and '03, the company sold its transmission and D&R arms for \$3 billion and then spent \$4.5 billion to increase its electricity-producing capacity by 40 percent as it refocused as a wholesaler. It now serves only major customers in Canada (Alberta and Ontario—which are 64 percent of its total market), the U.S. (25 percent), Mexico (6 percent), and Australia (3 percent). And it's generating healthy profits (\$199 million in 2005). One of the people helping to shape TransAlta was Jim Dinning, now one of the prime candidates to replace the retiring Alberta premier, Ralph Klein. Jim had been provincial treasurer when he joined the company in 1997, and he became executive vice-president responsible for sustainable development and external relations. He would concentrate on clean-coal technology and other long-term initiatives until leaving to focus on his political future in early 2005.

The corporation has a strong board now, chaired by Donna Soble Kaufman, a well-known Toronto lawyer, former head of Selkirk Communications Ltd., and director of Bell Canada, TransAlta, Telesat Canada, and the Hudson's Bay Company. Donna still sometimes calls me for a bit of private counsel on governance issues and the chair's role. "We are firmly committed to an ethical culture and good corporate governance," she says. TransAlta was named in a KPMG/Ipsos Reid poll as one of Canada's ten most respected companies, the *Globe and Mail* called it one of the country's best-governed corporations, and the Canadian Institute of Chartered Accountants has consistently honoured it for its financial and corporate reporting. Like TransCanada, it's investing in alternative-energy technology like wind farms. As the *National Post* has pointed out, "With energy prices and energy utility markets soaring in the U.S. and Canada, TransAlta Corp. is positioned for growth." My guess is that someday it might be one of the biggest power merchants on the continent—a possible Northern Tiger.

THOUGH I LEFT TRANSALTA'S board in 1998, I was still spreading myself thin on the boards of other companies, among them Crestar Energy, operating out of the Dome Tower in Calgary. I was one of the original directors when Crestar was created six years earlier by the Canadian subsidiary of Amoco Petroleum of the U.S.—which in taking over Dome Petroleum had promised Ottawa it would let Canadian investors own 20 percent of Amoco Canada Petroleum. As things turned out, it decided to launch a domestic company instead, built on assets owned by Amoco, Dow Chemical, and Encor Inc., TransCanada's upstream oil and gas subsidiary. The promising new venture, which I felt had at least an outside chance of evolving into a Tiger one day, would survive on its own for only eight years. Its demise would have one major lesson for those who want to create Canadian corporate champions.

Crestar's founding president and chief operating officer was Murray Todd, a thirty-six-year veteran of the industry. He'd been president of Dome's offshore-exploration division, Canadian Marine Drilling, and after the takeover, became a VP of Amoco. He was now in charge of a lean, privately held operation with about three hundred employees—about two-thirds of them from Dome—and four hundred thousand hectares of decent Alberta resource leases, much of them on former Hudson's Bay Oil and Gas lands. In 1993, Crestar was being prepared for an initial public offering in which Amoco and Dow, honouring their pledge to Canadianize the company, would sell their shares to domestic investors. Murray's strength was as a driller, not as a dynamic CEO. The board asked him to take early retirement.

His replacement was Barry Jackson, president and CEO of Northstar Energy Corp. and other smaller public companies. Don Stacy, Amoco's president and Crestar's chairman, had decided Barry was the best candidate. When I complained that I didn't know the guy, Don said, "For God's sake, Haskayne, he worked for you at Hudson's Bay." Unknown to me, Barry had been with HBOG as a junior engineer. He proved to be a fine choice: level headed, technically skilled, and a good public speaker. He did the

IPO and, under his leadership, a \$6.9-million loss in the first ten months of Crestar's life turned into a \$5.7-million profit in 1993.

We had an interesting group of directors backing him—among them, Roland Priddle, ex-chairman of the National Energy Board; Murray Fraser, president of the University of Calgary; and my suggestion, sharp-eyed Harry Schaefer, who became chair of our audit committee. But all of us—board members and management—were facing the same challenge: We had a nice enough company, but it was a Mr. In-Between. While it had some heavy-oil prospects and an okay natural-gas base, most of its assets were old ones in southeastern Alberta where production was declining rapidly. Crestar didn't have a growth story to tell. By now, it had 550 employees and a daily production of forty-three thousand barrels of oil and 351 million cubic feet of natural gas. Yet it just wasn't big enough to rank among the senior producers but was too big to be considered a junior. And many investors, especially Americans, preferred larger companies and thought that anything under \$10 billion was a small-cap venture. Crestar eventually did try to expand internationally, buying \$142 million worth of producing assets in Ecuador. But that wasn't enough of an attraction.

So in 2000, this mid-sized company was a ripe prospect for a takeover by a senior producer—Gulf Canada Resources. Years earlier, after the Reichmann brothers had to relinquish control of their Gulf shares to a consortium of banks, the company was sold to a consortium headed by the swashbuckling Houston entrepreneur J.P. Bryan. A classic Type-A personality, J.P. (James Perry) was a lawyer who'd studied art history and worked in the rare-book business before doing deals on Wall Street as an investment banker and then launching a company in Houston that bought and managed oil investments for institutions and corporations. Because he was a lover of all things western, we used to call him "Texas—all hat and no cattle." He was a delightful guy to chat with over dinner, but was always shooting from the lip. He once told a Canadian Senate committee that it was too bad that, under federal law, Gulf had to have so many Canadian directors, referred to corporate governance as "just a load of guacamole," and said Canada should

ship all Quebec's hardcore separatists to France—just the kind of diplomat you want running a respected Canadian business. In 1994, J.P. was among a group that paid \$30 million to buy control of Gulf. He became president and CEO and soon cut 40 percent of the staff, bought a \$9.3-million Challenger jet, and moved the executive office to Denver. (Meanwhile, his chairman, Earl Joudrie, was convalescing after being shot by his estranged wife, Dorothy.) All this was going on while oil prices were sinking and the corporate debt was climbing to \$2.7 billion. Four years later, his board ousted Bryan.

His successor was Dick Auchinleck, a good engineer, a twenty-two-year mainstay of the company, and a hell of a lot less flamboyant than his predecessor, thank God. He sold the jet, brought the executives back to Calgary, and began retiring the debt while selling off Gulf's majority share of holdings in Indonesia. If J.P. was "the gunslinger," people called Dick "the mechanic" (and in fact, he fixed vintage cars as a hobby). In 2000, looking to grow and perhaps fend off takeover bids, he approached Barry Jackson with a friendly \$2.3-billion offer in cash and Gulf stock to buy Crestar. The combined oil and gas producer would be the seventh-largest independent in North America. An analyst told Dick it was a case of two ugly ducklings turning not into a swan, exactly, but at least into a stronger duck.

For our shareholders, the deal would make a heap of sense. As petroleum prices rose, the company was stuck with a big income-tax charge and Gulf was prepared to assume Crestar's \$565-million debt. The sad reality was that if our board didn't accept this amicable offer, there were some unfriendly ones very likely lurking just over the next hill. For all the reasons I've mentioned, a mid-sized company like ours with well-tapped properties was a natural target for takeover, quite possibly by a foreign acquirer. The simple lesson: Unless you occupy a very special niche in your industry, you'd better grow big enough to be predator-proof. Our board approved the deal. A couple of our directors, including Harry Schaefer, became Gulf directors. Having had my heart bypass only a year before, I happily *didn't*.

Yet I did watch, with concern, what happened only a year later. Dick's executive VP of business development and general counsel was Henry Sykes, a long-term mergers and acquisitions lawyer with the Calgary office of Bennett Jones. So in 2001, Henry was primed to entertain a bid from the folks who once controlled Hudson's Bay Oil and Gas when I was there: U.S.-based Conoco. After selling HBOG to Dome Petroleum, Conoco had slipped back into Canada in a minor way and, frankly, what bothered me was that they were poor corporate citizens, stinting on their charitable donations and community involvement. Now, in what would be the costliest takeover of a Canadian petroleum company, Conoco was making its Canadian presence felt with a big splash. It paid \$9.8 billion for Gulf and the remnants of Crestar.

Dick Auchinleck went on the board of Conoco Canada Resources Corp., and Henry Sykes, who'd fashioned the agreement, became president. But gone from the scene were two Canadian-owned petroleum producers: Crestar, a wannabe with a legacy of historic HBOG holdings, and Gulf Canada, one of the older and more storied public enterprises in the Oil Patch. And there'd be one more change of proprietorship: In 2002, Conoco Inc. and fellow American Phillips Petroleum Inc. merged to create an oil and gas leviathan that owns the renamed ConocoPhillips Canada Resources Corp.

At the time, Barry Jackson, who was on the Canadian corporation's board, was quoted as saying, "A lot of those same properties and, interestingly enough, a lot of the same people have moved right from the HBOG days through all of those companies and now back to Conoco. So, there is the circle."

True enough, I agree with my friend, but given that effective control of the company now rested with its American parent, another prospective Northern Tiger had bit the dust.