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Successfully Managing the Integration of Mergers and Acquisitions

E. Craig McGee, Ph.D.

Abstract

Despite their prevalence, few mergers actually achieved the expected results. This paper describes the critical factors for successful mergers. Some of the factors include:

■ Conduct a thorough assessment prior to the merger

■ Create an integration task force

■ Maintain visibility of leaders from both organizations

■ Understand the business metrics of both companies

A checklist of critical tasks to complete is provided.

During the 1980's and 1990's the numbers of mergers and acquisitions dramatically increased. As organizations were forced to restructure and develop new strategies to maintain competitiveness, mergers, strategic alliances, and other integrative organizational strategies became more prevalent. But a study by Rohrer, Hibler, and Replogle (a management consulting firm) found that 65% of a sample of merged companies called the outcome disappointing or a total failure. The question to be answered in order to increase the success of mergers or other partnerships is "How do we successfully integrate with another company whose values, culture, management approaches, and operating practices are different from ours?" Below are listed some of the factors that are associated with successful integration.

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Identify and support the core competencies and competitive levers of the partner company.

Executives of both companies should ask "What is it about the other company that led us to this arrangement?" Often the answer to this question is a core competency or body of technology that needs to be protected. The other question they should ask is "What is it about the other company that represents a competitive advantage?" Once these areas are identified, conscious decisions can be made to ensure that they are not minimized during the integration process.

Conduct a thorough organizational assessment prior to negotiating and closing the partnership agreement.

Most companies carefully inspect the financial performance and product suite of the partner company. They want to ensure that the partner company is financially viable and has a product set that is compatible with theirs. However, less attention is given to other aspects of the partner company such as:

- technical competence of the workforce
- organization culture and values
- metrics used to guide the business
- management styles and values
- information systems
- interpersonal styles

These are critical subjective areas that often make or break successful integration. Consider the clash in cultures between General Motors and Electronic Data Systems. It took over ten years for those organizations to integrate. Some people would argue that they never truly integrated and that is what led to the spinoff of EDS off from GM.

Develop a high-level integration plan during the negotiations of the partnership agreement.

Based on the organization assessment, due diligence and other assessment work that occurs prior to the formal closing of the partnership agreement, executives of both companies should be able to develop a high level plan for how the two companies will operate after the merger/partnering agreement.

After the announcement of the partnership agreement, quickly communicate to people what will change and what will stay the same.

Employees of both companies will naturally have a number of questions about new organization structures, new reporting relationships, geographic locations of new/merged units, etc. The plan developed during the negotiations can be an invaluable tool for allaying fears and concerns of people. Be frank, candid and understanding. Without a clear understanding of what the direction and plan is, people will create their own reality. They will spend more time creating that reality in their own mind than performing constructive work. In the absence of clear information, rumors will develop and spread. Executives and managers of both companies will spend more time controlling rumors than attending to the true needs of the business.

Create an integration task force.

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Even with a high-level integration plan, there remains a great deal of "detail" work to execute that plan. The execution of the integration plan is actually a 4 - 18 month process that must be carefully managed. And mid-level managers who can be most threatened by the new partnership, yet know the most about the day-to-day operations needed to support that plan, are an invaluable resource for executing that plan. A task force charged with working out the mechanics and logistics of the merger/partnership working relationships plays an important role.

Members of the integration task force should possess greater than average leadership, problem solving, and communications skills.

Consider that these people will be the ones who interact with the other company the most. Having the best and brightest people work on the integration will create greater confidence in the other partner and minimize unnecessary intrusion.

The integration task force should work closely with the senior management of both companies. In many cases, several of the senior managers will be active, full-time members on the task force. A senior manager who was deeply involved with the preliminary discussions and final negotiations should be a member and/or leader of the task group. This manager should be knowledgeable about the general intent and discussions that occurred during the negotiations and ensure that the execution of the integration plan is consistent with those discussions.

After the merger/partnership agreement has been signed, the leaders of the parent company should be highly visible on the site of the purchased/merged company.

Activities should be designed that enable the new employees to get to know them and their management philosophies. These activities include planning sessions, communications meetings, Q&A sessions, informal forums, roundtables, picnics, etc. This is not a one-shot exercise. There should be a series of events to allow the employees to get to know the managers/executives of the parent company better.

Conversely, it is important that the managers and executives of the acquired company establish a presence within the parent company.

It is important that they protect structures and practices that have led to their success. They should visit the parent company's main office to review operating plans, strategies, and major project status. It is important that they project an image of competence, confidence and cooperation.

Utilize large group methods to integrate cultures.

Cultural differences between the merging organizations can significantly impact how effectively the post-merger organization operates and delivers the business results upon which it was justified. Large group methods effectively eliminate the fear and anxiety associated with mergers and focus all employees on the strategic objectives required to achieve the desired synergy. These methods serve as effective communications vehicles to keep people aligned.

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Effective working relationships need to be built at all levels of the organization.

It is common for the senior managers who negotiated the partnership agreement to have developed a strong, cooperative relationship. However, managers at lower levels of the organization tend to protect existing turf. The integration task force is one means for building the same cooperative working relationships throughout the two companies. Additional task groups can be formed to resolve the myriad of integration issues that arise and provide a mechanism for building these relationships among other people in the two companies. The task groups should be chartered by the integration task force and report to them during the integration process.

Process mapping is an effective tool for helping managers from the two different companies understand the operating practices in the other company. It identifies the points in the process where integration must occur. It identifies redundancies and opportunities for streamlining existing processes. It identifies information system requirements. Process mapping will typically surface conflicts in roles and responsibilities among the managers and work groups in the two companies. The quicker these role conflicts are identified and clarified the quicker the integration proceeds.

Teambuilding among the new groups can also be helpful. Efforts should be made to create or identify tasks around which to structure group activities. Successful accomplishment of meaningful tasks builds effective work teams. Examples of tasks include:

- merging the information systems of the two companies
- evaluating the benefit plans of the two companies and integrating them if necessary
- integrating the product plans of the two companies
- clarifying the structure of the sales force and technical support

A group should also be chartered to listen for rumors and respond to them quickly.

This is often the responsibility of one of the subgroups of the integration task force. This group is comprised of employees who are well respected and have good working relationships with their peers. They will be able to hear rumors during their early stages and prevent the spread of inaccurate rumors.

The attitude of managers and executives of both parties should reflect one of problem-solving, cooperation and equality rather than condescendence, superiority or defensiveness.

Senior managers of both companies will need to closely monitor the activities at lower levels of the organization to ensure that the proper tone and attitude is being promoted. Again, issues of turf protection and colonization can be very prevalent and must be carefully guarded against.

Sweat the big stuff.

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Do not allow managers and executives to compromise those core competencies or operating practices that have made each of the companies successful in their own respect. Senior managers should be prepared to strongly resist changes they believe will weaken the core competencies or technologies.

Similarly, help people turn loose of the minor issues. Long standing practices may no longer be supported by business rationale. New practices may produce economies of scale and greater synergism. Effective communications will help people understand the differences between old practices for old practices sake and new practices for greater synergism.

Allow for differences.

There are already significant differences in management style, levels and roles of management and implementation of policy among different departments in the same company. Diversity among practices and policies may actually be the engine for organizational innovation. Unless these differences produce glaring violation of corporate policies and operating inefficiencies, they should be considered.

Understand the business metrics used by both companies.

The metrics used for evaluating business unit performance have profound effects on the organization. They affect staffing, product planning, marketing program development, etc. The business metrics used by one company may directly conflict with the metrics of the other company. Implementing the metrics of one company in the other may severely compromise the core technology or undermine the core competencies of the organization.
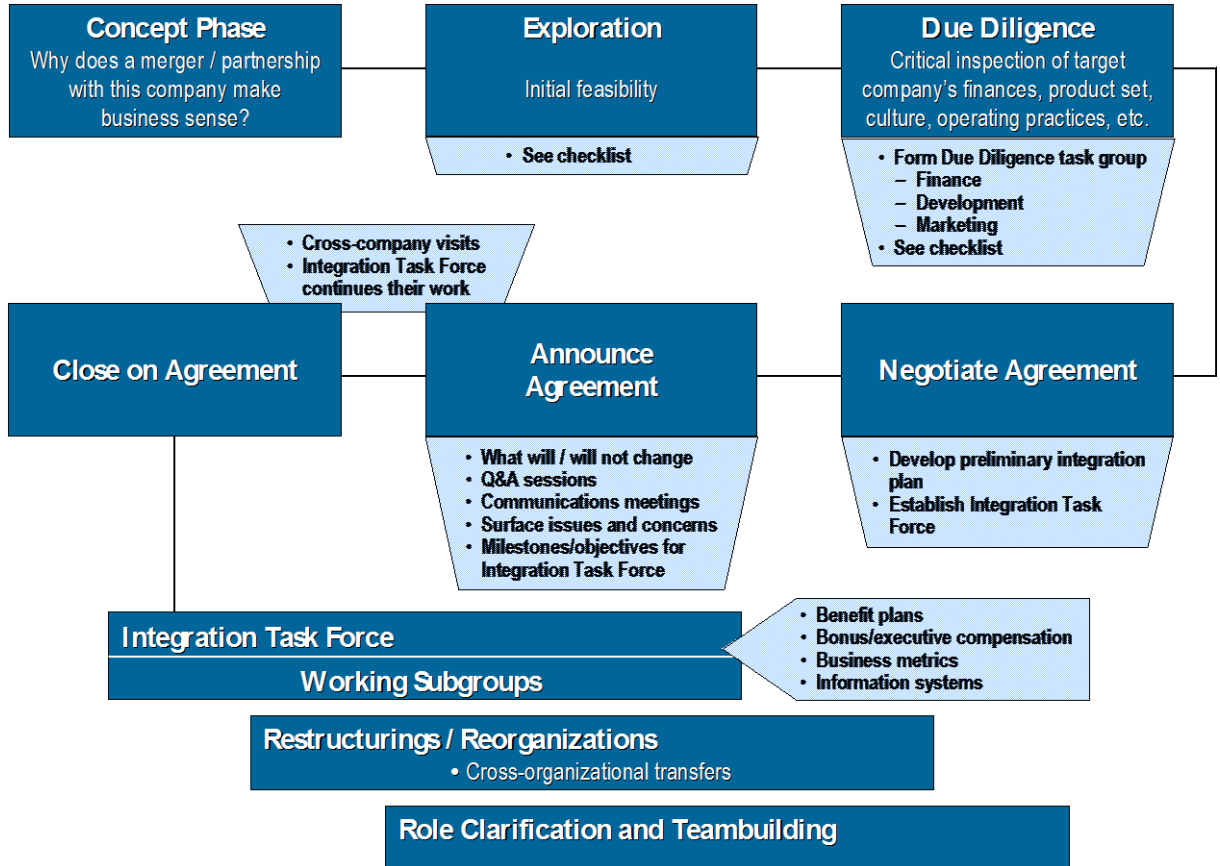
For example, consider an acquired company with a core competency of technical expertise and the ability to develop products with cutting edge technology. Supporting this core competency requires extensive training and development costs, attendance at professional meetings and networks, support for university research, etc. If the parent company uses metrics that emphasize cost control, it is likely that these expenses will be reduced, thereby diminishing the core competency over time.

Encourage and promote cross-company transfers.

It is very common for the parent company to transfer new managers and executives into the acquired company. This helps diffuse the values and operating practices of the parent company into the acquired company. However, less common is the transfer of managers and executives from the acquired company to the parent company. Successful integration requires advocates for the acquired company who are embedded in the parent company's management system.

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Merger and Acquisition Integration Process

Concept Phase
Why does a merger / partnership with this company make business sense?

Exploration
Initial feasibility

- See checklist

Due Diligence
Critical inspection of target company's finances, product set, culture, operating practices, etc.

- Form Due Diligence task group
  - Finance
  - Development
  - Marketing
- See checklist

- Cross-company visits
- Integration Task Force continues their work

Close on Agreement

Announce Agreement

- What will / will not change
- Q&A sessions
- Communications meetings
- Surface issues and concerns
- Milestones/objectives for Integration Task Force

Negotiate Agreement

- Develop preliminary integration plan
- Establish Integration Task Force

Integration Task Force

Working Subgroups

- Benefit plans
- Bonus/executive compensation
- Business metrics
- Information systems

Restructurings / Reorganizations
- Cross-organizational transfers

Role Clarification and Teambuilding

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Merger and Acquisition Checklist

I. Concept Phase

A. What is it that this company can contribute to our company?

- Distribution channel
- Manufacturing capability
- Research and development
- Customers/accounts
- Product line
- Market segment (geography, industry, price point, etc.)
- Specialized technology
- Human capital
- Revenue stream
- Financial assets

B. what would be the costs to develop this capability on our own?

C. How long would it take to develop this capability on our own?

D. What is the synergism of the merger? How does this company complement ours?

E. What are the options for obtaining the capabilities this company has?

- Merger/acquisition
- Joint venture
- Joint marketing/distribution agreement
- Strategic alliance agreement
- Licensing
- Commission/royalty agreement
- Consulting services
- Patent/technology option
- Internal development

II. Exploration

A. Finances

1. What is the financial strength of this company?

- Assets
- Liabilities
- Revenue streams
- Strength of balance sheet

2. What are the financial projections for the next 1-3 years?

B. Current Products

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1. What is the current profit contribution for different product lines? What are the trends for profit contribution over the last 3-5 years?

2. What is the projected profit contribution for different product lines?

3. Where are each of the products in their product life cycle?

C. Future Products

1. What products are in the pipeline?

2. How do they complement the existing products?
   - Product line extension
   - New product line
   - New product family thin existing product line

3. When will the products begin generating revenue?

4. What are the projections for re venue/profit contribution?

D. Customers/Suppliers

1. Who are the current customers? How is revenue/profit contribution distributed among these customers?

2. Are there any long-term supply agreements? What are the basic terms of those agreements?

3. Who are the current suppliers? What do they supply?

4. Is any core technology supplied by outside vendors?

5. Is there any long term purchasing agreements? What are the basic terms of those agreements? Is there redundancy/conflict in the supplier chain between this company and ours?

E. Culture

1. What is the prevailing culture?
   - Bureaucratic (GM)
   - Autocratic (Exxon)
   - Entrepreneurial (3M)
   - Egalitarian (H-P)
   - High Performing (Tektronics)
   - Market drive/technology driven

3. What would be the potential cultural conflicts during integration?

4. What would it be like working with the existing managers/executives?

III. Due Diligence Examination

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A. Financial

    1. More detailed examination of financial records – all of the above plus:

- Patterns of maintenance and capital expenditures
- Patterns of marketing, sales, general, and administrative expenses (SG&A)
- Unexposed liabilities
- Valuation methods for assets
- Determination of goodwill
- Funding of pension plans

    2. Executive compensation

B. Legal exposure

- Pending, probable or possible litigation
- Trademark/patent protection/violation
- Environmental exposure (real estate, chemicals/materials, compliance record)
- Safety and health practices and exposure
- EEO/AA exposure
- SEC/shareholder rights exposure
- IRS/tax exposure

C. Visual/Onsite Inspections

D. Customer/Supplier Contracts

- Detailed examination of contracts (terms, length, termination provisions, etc.)

E. Current Product

- detailed examination of product lines
- breadth of product line
- functionality and capability of product line
- detailed examination of product components
- purchased/licensed technology
- purchased/licensed subcomponents
- where is the greatest value added?
- detailed examination of product life cycle (how mature is the existing product set)
- market performance of current products
- market perception of product line and capability

E. Future Products

    1. What are the future product plans

- extension of current product line (enhancements)
- new product line
- new product family within existing product line

    2. What resources have been allocated to future product development

- capital (equipment, buildings, or acquisitions)
- personnel (headcount)

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- technology

3. What further resources will need to be allocated for future product development and commercialization

G. Core Competencies

1. What are the core technologies of this company?

2. How do they complement our core technologies?

3. What are the other core competencies of this company?
   - customer service
   - distribution
   - data management
   - commercialization of technology
   - development of basic technology

H. Human Resources Administration:

1. What is their compensation philosophy?

2. How do their pay structures compare to ours? Will there be internal equity issues that we will have to address?

3. How do their benefit plans compare to ours?
   - health and medical insurance
   - vacation/holidays
   - pension
   - education reimbursement
   - leave/time off policies
   - stock purchase/options

4. Will we need to maintain separate benefits plans or can they be integrated with ours?

5. Is this company in compliance with major state and federal regulations?
   - EEO/AA
   - OSHA
   - ADA
   - wage and labor standards

J. Workforce Competency:

1. What is the technical competence of the workforce?

2. Where are the areas of technical competence and technical weakness?

3. What is the educational level of the workforce? Are there concentrations of well educated or poorly educated?

4. What are the social skills of the workforce?

5. What is the managerial competence level of this organization?
   - planning/budgeting
   - project management
   - leadership
   - financial stewardship

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6. Who are the key technical, managerial, and executive people? Why are they considered key? What would happen if one or more of them left?

K. Culture

1. Decision-making

   - what is the predominant style of making decisions?
   - who makes what decisions? with what input from whom?
   - what is the risk taking quotient?
   - how are failures/mistakes dealt with?

2. Cross-functionality

   - to what degree are individuals "functionally" bound?
   - are individuals generally promoted across functional boundaries or up through a singular discipline?
   - to what degree is there a functional/discipline loyalty?
   - are there cross-functional structures (Steering Committees, Project Teams, temporary teams, etc.)? How well do they work?

3. Reward Structure

   - what do people get formally rewarded for?
   - on what basis do people get promoted or otherwise recognized?
   - what is most important to this company?

4. Norms and Values

   a) What are the general norms of this company?

      - how are mediocre/poor performers dealt with?
      - to what degree is conflict encouraged or tolerated?
      - what are the typical responses to conflict?
      - how well are deadlines set and met?
      - how detailed is project planning?
      - how is input from various parties obtained and used?
      - what are the general modes of communications (written, verbal, phone, etc.)?
      - how are various stakeholders dealt with (customers, vendors, employees, shareholders, unions, etc.)?

   b) What are the general values of this company?

      - market driven
      - quick response/flexibility
      - technology driven
      - 100% quality
      - outrageous customer support

   - technical leadership
   - respect for all employees
   - thoroughness
   - execution

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- creativity

IV. Preliminary Integration Plan

A. What areas of this company are unique and should be maintained? What are the core competencies we are trying to access?

B. What areas/competencies of this company are redundant with ours?

C. What is the appropriate structure for this relationship?
- merger/acquisition
- joint venture
- joint marketing/distribution agreement
- strategic alliance agreement
- exclusive partnering agreement
- licensing
- commission/royalty agreement
- consulting services
- patent/technology option
- internal development

D. What are the costs associated with the different options:
- purchase price
- buyout of current shareholders
- severance costs
- relocation expenses
- licensing fees
- commissions/royalties

E. Information Systems

1. What is the basic architecture of the information system? How compatible is it with ours?

2. What are the basic data models used? How compatible are they with ours?

3. What metrics do they use and how are they tracked? How compatible are they with ours?

4. What information systems/linkages will need to be established between the two companies?

V. Terms and Conditions Negotiations
- final agreement

Solutions Overview

Solutions is a management consulting firm specializing in meeting the needs of companies to improve operational performance. Drawing on a broad base of experience, Solutions consultants work with a client's management team to achieve major improvements in competitiveness, profitability, customer satisfaction, and growth. Applying analytic tools, state-of-the-art technologies, high involvement methods and best practices, Solutions helps clients develop strategies to surpass their business goals and transform their business enterprise.

The author, E. Craig McGee, Ph.D., can be contacted directly at 970-416-0809 or email: info@solutionsconsulting.org.

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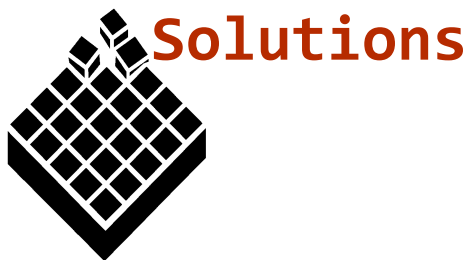
2017 Linden Lake Road
Fort Collins, CO   80524
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