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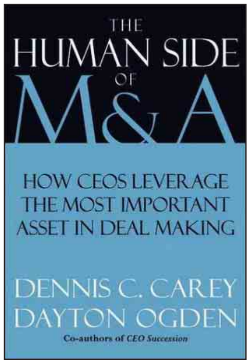

The Human Side of M&A

How CEOs Leverage the Most Important Asset in Deal Making

by Dennis C. Carey and Dayton Ogden
Oxford University Press © 2004
208 pages

Focus

- Leadership & Mgt.
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Take-Aways

- Mergers and acquisitions continue to be strategic options. That is not likely to change under current economic and industry conditions.
- Human capital is a fundamental but often neglected component of merger success.
- Strategies and plans are useful only when a management team can implement them.
- Corporate culture is the product of decision-making, metrics, compensation, technology, values, attitudes, employees and focus.
- Chief executives should have – and share – a clear vision of the merger mission. Make sure everyone involved understands the vision.
- Retention of important talent is a critical challenge.
- Ambiguity is the enemy of merger integration.
- Regulatory decisions, which can make or break mergers, are often illogical.
- Integrate as expeditiously as possible. However, taking too many steps toward integration before you receive regulatory approval can be imprudent.
- On a new merger, prioritize creating a corporate governance structure.

Rating (10 is best)

Overall	Applicability	Innovation	Style
7	8	6	7

Relevance

What You Will Learn

In this Abstract, you will learn: 1) Why some mergers succeed and some fail; 2) How corporate culture may determine whether a merger succeeds; 3) Which "human factors" to consider when negotiating a merger; and 4) Why you should use incentives to retain executive talent.

Recommendation

During the 1990s, mergers and acquisitions (M&A) hit a historic high. Yet academic research confirms what anecdotal evidence suggested: most mergers do not work. Authors Dennis C. Carey and Dayton Ogden (writing with Judith A. Roland) contend that most mergers fail because of mismanagement and neglect of the merged company's "soft side" – the cultural and human dimension. They draw on their experiences as human resource consultants to outline a strategy for assessing people, creating vision, integrating mergers and addressing the soft side's hard problems. *getAbstract* finds that the book's greatest strength is its interviews with executives and other insiders who have direct experience with high-profile mergers, both successes and failures. If you are an executive or human resources manager in a company on either side of a merger – or if you think you'll find yourself in that position in the future – read this book before you sign that deal.

Abstract

"It doesn't take a business historian to grasp the lessons from failed mergers of the past."

Why Some Mergers Succeed

The world has never seen merger-and-acquisition activity on a scale comparable to the frenetic pace of the 1990s. Yet, according to some estimates, more than two-thirds of announced mergers fail to take place, and even when they happen, they are less profitable than anticipated. The success of a merger hinges on the following critical elements:

- Sound strategy – Merger or acquisition must be the appropriate strategic response to the business situation.
- No hidden pitfalls, traps or dangers – Insist upon thorough due diligence to ensure that no previous legal or accounting issues will cause problems in the future. Conduct "cultural" due diligence as well.
- Human capital – The right people must be in place and able to do the job.

"The key challenge for the merging organizations is to take stock of a full menu of human capital issues quickly in a regulatory environment that makes it difficult in the face of delays, rampant uncertainty and a high degree of anxiety at all levels."

Follow these guidelines to minimize your risk and improve your long-term prospects for a successful merger:

- Make your goal clear – As a leader and manager, you should have no doubt about the purpose of the merger. Establish milestones. Check progress regularly so you know if the merger is going in the right direction.
- Believe – Have faith in the merger, make a personal commitment and evangelize to recruit other true believers.
- Reach out to the operations side – The decision to merge is strategic, but you need support from operating executives for it to succeed. Include operations in planning.
- Know who's on first – Involve leaders from the earliest stages of the process.

- Never forget that corporate culture is crucial – If the CEO and other leaders focus only on the numbers, so will the troops. Communicate the importance of culture to everyone involved, at every step.
- Involve human resource management – Because "soft" issues are so important to merger success, involve human resource managers in planning.
- Second-guess the CEO – Some CEOs do deals because they like to do deals – but the excitement of dealing is not a good reason to go forward with a merger or acquisition. The board should ensure that the reasons leadership gives for the merger or acquisition are indeed strategically sound.
- Recognize the value of the alien culture – Culture may be an important component of an organization's competitive success. In such cases, maintain a sort of "cultural reservation" for certain business activities, even if this means some units stay relatively independent from the rest of the acquiring or merged organization.

"The world's best strategy and projections mean little if a company does not possess a management team capable of carrying out well laid plans."

Human and Cultural Factors

Not surprisingly, cultural incompatibility is one of the main reasons mergers fail. Analyzing culture is time-consuming, yet mergers often occur on a fast track, leaving you without much time to dig up and analyze hard-to-get information. As a result, executives lack the information they need to ensure the transaction's success.

"The CEO's view is likely to be the most comprehensive, so it is bound to differ somewhat from anyone else's in management, even those who may be part of the top management team."

Organizational culture determines the behavior and decision-making strategies of most executives. But during a merger, culture necessarily changes. Your goal is to create a new synthesis, not to have one corporate culture eliminate the other.

Mergers succeed or fail based on human capital. If you don't manage your human capital correctly, your deal will not succeed. Managing a merger is difficult and complicated; no easy-to-follow recipe can ensure success. Still, planning for every possible contingency and following through completely will improve your chances.

Retain Your Best Talent

The best plans are useless without the people to implement them. When you oversee a merger, recognize that the management teams in both organizations are key, and assess them carefully. As a leader facing a merger, your first task is to audit your human capital. Executive recruiters use the techniques and tools of human capital audits when they conduct searches to fill high-level executive posts. Don't trust appearances as you get to know the other firm's team – some of the best executives are quiet and unassuming.

"Setting up and evaluating a human balance sheet is a tricky proposition, but that is what we recommend companies do when contemplating a merger."

Your clear understanding of the business reasons for the merger will determine who should stay and who should go. Ultimately, the executives best able to achieve the business goals should stay.

Compensation and bonuses can create important material or monetary incentives for executives to remain with the company. However, money alone will probably not be enough. Most people consider quality of life and company culture as they make the decision whether to stay or go.

"Beyond the facts and figures that may indicate a good match, careful attention must be paid to corporate cultures and how they're likely to match."

Take the following steps to retain necessary executive talent:

- Recognize and deal with high anxiety – The stage between announcement of the merger and consummation of the deal is nerve-racking.
- Communicate – Clarify the business case for the merger, over and over, to everyone involved in both companies.

- Let strategy guide your human capital decisions – Decide on retention and termination based on which talents you need to make the merger a success.
- Establish incentive programs – Target the people the company wants to retain.
- Make culture clear by your actions – Demonstrate your corporate culture through your compensation programs and severance offers. Be sure that you transmit the message you want people to receive.
- Let the Golden Rule be your guide – If you expect personnel from the company you acquire to work as your teammates, don't treat them as conquests.
- Emphasize understanding – Leave no doubt about what is happening and why, especially if employees will feel the change in their pay envelopes.
- Establish fair compensation systems – Salaries should be rational and equitable.
- People are central – The success of the merger depends on having the right people in the right places.

"All roads lead to the strategy, the business case."

"For mergers that are subject to regulatory approval, the process can exact quite a toll, on a human level as well as a business level."

Integrate Quickly

Integration should be prompt and decisive. The CEO can be a unifying force in bringing different groups together and helping to defuse conflicts. Thus, the CEO should see and be seen throughout the newly merged organization.

To proceed with integration, follow these guidelines:

- Put the CEO front and center – The CEO's direct, personal involvement in planning and decision-making is indispensable.
- Have a battle cry – Express the vision in a slogan that you can drive through the entire organization.
- Designate one leader with a clear message – Leadership is essential for communicating the vision and the message.
- Oppose equivocation – Leave no doubt about who is in charge and for how long.
- Don't let the most important people leave – Give them real incentives to stay and provide them with "parachutes" in case the merger doesn't work.
- Tailor your model – When merging different organizations, make changes in the previous messages and models.

"The limbo period when the company is going through change, whether it's integrating another entity or a full-scale transformation, is the time of high anxiety for all involved."

The Regulatory Gauntlet

One of the most perplexing merger misadventures of the 1990s was the failure of the merger of Staples and Office Depot. Even after the companies took the steps recommended by the U.S. Federal Trade Commission staff, FTC regulators turned down the merger, for reasons that are still unclear. Regulators can be unpredictable that way and, "there is never a guarantee of approval until it happens."

Dilatory or inconsistent regulation can cause severe problems for merging companies. For example, once you tell employees that they will be laid off because of a merger, they are unlikely to resume working with the same degree of diligence and confidence, even if regulators fail to approve the merger and you go back to business as usual. When you're involved in a merger, consult with experts who understand the ways of regulators, have contact people within the relevant regulatory agencies and can help your organization satisfy regulators' demands.

"If the new company is to get off to a running start, the integration process must begin well before the new entity gets the green light to operate as one company."

Remember the following points:

- It ain't over till it's over – Do not integrate prematurely. Approval is not final until it is signed, sealed and delivered.

- Wait for regulatory approval before appointing new management – Executives who discover they won't be part of the new company may leave, creating gaps in the ranks if regulators veto the merger.
- Move quickly – Despite regulatory delays, move expeditiously as soon as motion is prudent. Do not make any irreversible announcements when the regulatory approval is pending, but once regulatory approval is probable, don't allow anxieties and doubts to linger.
- Use incentives – Strategize about retaining important talent even as the regulatory machine grinds through its process.
- Get good advice – Understand what regulators have in mind and how you can cooperate with them.

"Major mergers and acquisitions present a number of opportunities to build a better board that will not only help the company during the deal but will also serve as a resource going forward."

Governance in an M&A Environment

Corporate governance is more important and more challenging than ever. Recruiting good directors can be a challenge. Because board members serve for years and may be difficult to change, look at the merger as a new beginning. You can often find talent on the boards of acquired companies – and the directors of an acquired company may be disposed to join the acquirer's board. However, avoid simply combining the boards of both companies. Boards must be nimble, and large boards move slowly.

The following are a few governance do's and don'ts:

- Do learn about best governance practices – Use the merger to align your company with the best practice.
- Don't use simplistic board selection techniques – Or you'll end up with a board stocked with mediocrities.
- Do examine the skills and expertise of each board member – Select board members who have the particular skills that you need.
- Do look right in your own back yard – In other words, examine the acquired company's board. Even if you have no obligation to bring on those directors, their strengths and intelligence can be quite valuable to you. Moreover, reaching out to them, especially when you don't have to, can create an enormous amount of goodwill.

"Some companies seem determined to learn from past mistakes; others seem destined to repeat them."

Who Benefits?

Because mergers so frequently fail to produce the synergies everyone hopes for, the premium that the acquiring company pays for the acquired company amounts to a transfer of wealth to the shareholders of the acquired company. Thus, according to the financial literature, acquisitions most often benefit shareholders in the acquired company.

The shareholders of the bidding company usually do not receive any statistically significant positive returns. Nevertheless, careful attention to the human side of M&A, cultural due diligence, and prudent management of the soft factors can help you beat the odds and make a merger soar.

About The Author

Dayton Ogden is the chairman and Dennis C. Carey the vice chairman of a leading executive search firm. They are co-authors of *CEO Succession*.