M&A Done Right

By Rick Warner

Information technology resources should be an upfront consideration in managing mergers and acquisitions. Failing to do so can result in setbacks down the road.

Ensuring a successful merger or acquisition and achieving the expected benefits is one of the most critical challenges businesses face. Global deal volume was estimated at nearly $4 trillion in 2016, meaning there is more M&A activity occurring than ever before. Some deals are driven by the desire for increased scale in the marketplace, others by enlargement of scope.

Regardless of the rationale, they have one thing in common: It is vitally important to all concerned that they succeed. M&As have high visibility—and high pressure to perform. Careers can be harmed if they fail; the stakes are high. However, when all is said and done, fewer than half of all M&A activity is thought to return positive value. Why? And how can this be improved?

I have been around a substantial amount of M&A activity—sometimes on the acquiring side, and other times as the entity being acquired. Because my area of focus has been information technology, I have seen time and time again how critical—and difficult—it is to get this piece right, even under the best of circumstances. IT is often the single largest cost component associated with any deal. However, it is also a potential change agent to fundamentally affect how business is done going forward.

Most deals fail because not enough time is spent up front determining whether a deal should be done in the first place. Why does it make sense? What issues are in play? What are the risks? This is especially true when it comes to IT engagement. Too often, it's an afterthought. Dealmakers tend to think, "There is no reason to involve our (relatively scarce) IT resources until things become more serious. Otherwise, if the deal falls through, it would be a waste of time."

This perspective can be a big mistake. The overall effort associated with M&A tends to be underestimated and understaffed—especially in the early stages. It is often a complex and time-consuming event that needs to be undertaken by a tightly integrated team of some of the "best and brightest" people in the company. Will that affect day-to-day operations? Possibly, but proper planning can address that. Operations would be far more affected later if the integration effort associated with the deal is done poorly.

Usually, deals result from external factors such as pressure to grow, unexpected new market opportunities, concerns that a competitor might act first, etc. Typically, the window for evaluating potential M&A candidates is short. Often, some level of prequalification as to whether a deal would be a good strategic fit has already happened at the senior leadership team or board level. Generally, a hastily organized vetting process is then put in place to confirm initial impressions (with a bias toward validating why a deal would work, rather than surfacing true red flags).

The pressure to act quickly may result in potential obstacles being overlooked. Projections are made and expectations set, based on very limited information and a lot of assumptions. If things look positive, the operating divisions (including IT) could be given the mandate to make it happen . . . along with everything else they are doing. If this is how an M&A is handled, key players will have limited control over their own destiny. Much of their activity will be reactive going forward. It is very difficult to succeed in this environment.

HERE ARE SOME BEST PRACTICES THAT HAVE BEEN ADOPTED BY WORLD-CLASS ORGANIZATIONS TO BREAK THIS CYCLE.

STEP ONE

There needs to be more emphasis on research, evaluation, and planning prior to closing the deal. In general, the four phases of M&A are:

- Due diligence
- Preparation
- Day-one execution
- Ongoing integration

If you look at where overall M&A effort is spent, a deal funnel typically looks something like this:

To be successful, the funnel really should be inverted to put increased emphasis on the first two phases (due diligence and preparation):

The intent is to ensure that issues are identified as early as possible and can therefore be addressed quickly. In some cases, additional vetting could result in walking away from a deal altogether. That is not necessarily a bad outcome; sometimes the best deals are the ones that never occur. Also, if the first two phases are done correctly, less time will be required down the road because much of the reactive scrambling to address unwanted surprises will not be necessary.

STEP TWO

Consider IT early and often in the M&A process—not as a secondary concern in planning the deal. IT time and cost estimates will be a big part of the ultimate valuation, so they must be as accurate as possible given prevailing constraints. No assumptions around system consolidation (and associated cost savings) should be made without IT's sign-off, which requires IT representation at the table when these are first discussed.

STEP THREE

Form a deal team, which includes business analysts, finance people, legal support, and IT. This team should be composed of seasoned resources—in the case of IT, the CIO, or a designated direct report. Avoid the temptation to include junior or "less busy" people because their absence would minimally affect ongoing operations. Rather, assign the best resources available and temporarily backfill their positions with contractors or consultants as needed. Prepare for an appropriate hand-off after the deal closes and integration tasks are assigned to others. That means members of the deal team should not resume their normal role overnight without ensuring proper continuity.

STEP FOUR

Put a governance structure in place with clearly defined roles for communication, decision-making, and escalation purposes. Develop appropriate messaging and consider the optimal means to reach the many affected audiences (e.g., deal team, senior leadership, acquired employees, affected customers, etc.). Quantify cost-saving opportunities and track them over time. Perhaps most importantly, establish overall goals for the deal. Otherwise, it will be difficult to determine what success looks like and how it will be measured. If feasible, establish a separate PMO just for the deal, with a dedicated, highly skilled program manager.

STEP FIVE

Along those same lines, adopt a structured methodology/approach. This is especially important during due diligence so nothing falls through the cracks. The use of a third-party M&A framework to guide activities, avoid omissions, and prevent other pitfalls is highly advisable. More on that later.

STEP SIX

During due diligence, consider the evaluation of people, process, technology, culture, spending, and vendor contracts to be within scope. With limited access to the right resources at the acquired entity, all of the key players need to be promptly identified, and good questions need to be developed for them. Within an M&A framework, existing templates can provide a "starter set." When given the opportunity, be sure to visit data centers, as well as a representative sampling of the various points of distribution (e.g., warehouses, stores, etc.). Take lots of pictures. Do not rely solely on reports and paper representations. There is simply no substitute for "putting eyes" on the situation. Collect and review all IT/telecom service agreements with your legal department. This step is often overlooked, but failure to do so can really come back to haunt you. Quantify and evaluate the cost of breaking existing contracts.

STEP SEVEN

Part of the review process is to evaluate the acquired entity's existing IT staff. Assess which staff members are "keepers," and incentivize these individuals to remain on board with a retention bonus—at least through the transition period, if not beyond. The CIO of the acquiring company should really be thinking about how the IT organization of the future will look, and how key players from the acquired company might fit in.

STEP EIGHT

From a planning perspective, pay special attention to anything that needs to be in place immediately following the deal closing (day one). Priorities include separating financial ledgers so daily transactions are properly recorded, compensating people as appropriate, facilitating communications to and from the new parent company, processing payments, ordering supplies, and rebranding anything that is customer-facing. This typically entails finding a way to provide quick access to the acquiring company's corporate systems, such as accounting, payroll, email, procurement, etc. Also, deals rarely close exactly when expected. Last-minute things come up, which can delay closing by hours or even days.

STEP NINE

During day one transition, minimize the impact on overall customer experience. The transition must occur with as little perceived downtime and disruption as possible. Schedule system cutovers to occur after normal business hours, if possible. While it is tempting to view any transitional downtime as an ideal time to implement improvements and do some re-engineering, the first rule should always be "do no harm." IT must restore customer-facing operational functionality as soon as possible. Prolonging an outage by trying to do too much will not be well received.

STEP TEN

That said, failing to consider how to achieve synergies and leverage new technology would be a missed opportunity. IT is in a unique position to identify potential wins on behalf of the business. The trick is to incorporate these in such a way that the core day one activities are either unaffected or folded in later.

STEP ELEVEN

Typically, the default approach is to replace the acquired entity's systems, processes, and in many cases, people, with those of the acquirer. This is not necessarily because what the acquired entity has in place is not as good. Instead, the decision could be based solely on factors such as having to retrain a smaller group of people. There are exceptions, though. Going in, keep an open mind. This is especially true during a merger of equals. In this case, it is important not to be viewed as taking a step backward. So, replacing everything in sight is not always best. A better approach might be to attempt to repurpose resources and assets. This is especially true when it comes to hardware and network infrastructure.

STEP TWELVE

Timing is important. Often, the faster the overall integration effort can occur, the better. The theory is that the longer it drags on, the more people lose focus and the perceived value of the deal is reduced commensurately. However, the incremental costs associated with speed may be too great. For instance, some service contracts have significant penalties if they are terminated early versus letting them run their natural course and expire. In this case, it may make sense for the new buyer to assume responsibility for such contracts—even if the service provider is not one the acquiring company would normally use now or plan to use later.

STEP THIRTEEN

In any M&A situation, frequent and transparent communication is key. In the absence of a clear narrative, it is human nature to fill in the blanks in ways that range from inaccurate to disruptive. In the case of IT, this starts with the CIO communicating with peers on the senior leadership team. It is highly desirable for IT and the business to be aligned under any circumstances, but this is especially true during an M&A event. Also, the IT staffs from both the acquiring and acquired organizations need to be kept as informed as possible. Ultimately, most people will wonder, "What's in it for me?" so they must be advised and reminded accordingly. Culture matters. If the two companies coming together are significantly different in this respect, building a combined team may be challenging—but the added diversity could make it worthwhile in the end.

By now, it should be clear that M&A initiatives are inherently complex and ambiguous. Each situation is unique, so, unfortunately, there is no one-size-fits-all solution to ensure smooth execution. However, available tools can help mitigate much of the risk and uncertainty.

It is always advisable to use an M&A framework. Several exist—including one from Jabian called Value and Integration Management Office (VIMO™). Basically, a framework is a comprehensive model that provides organizational and operational structure. The VIMO™ framework also contains numerous templates and checklists, such as what key questions to ask when meeting with the acquired entity's IT department during due diligence.

This creates a process that directs activities and prevents important steps from being omitted. Whether you opt to use VIMO or a framework like it, going into an M&A initiative with a structured approach, sufficient time, and adequate resources will most definitely produce a better outcome.

Rick Warner
rick.warner@jabian.com

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