THE ROLE OF HUMAN RESOURCE IN MERGERS AND ACQUISITIONS (M&A): THE HAND THAT NURTURES!!!!!!

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ABSTRACT

Recent years have seen a significant rise in M&A activity, and Indian companies have played a crucial role both as acquirers and targets. Inorganic growth strategies like mergers and acquisitions have been championed by both Corporate Managers and Investment Bankers as important engines that help companies to grow fast, enter new markets, expand customer base, and acquire technology and expertise. Traditional wisdom would suggest that M&A’s should be able to unlock shareholder value through economies of scale and consolidation of assets and human capital. Research, however, shows that approximately 70 per cent of mergers and acquisitions fail to achieve expected results and about 50 per cent actually destroy value. While there are hundreds of reasons for the high failure rates of M&A, ranging from CEO ego satisfaction to incoherent due diligence methodology, a London Business School research points out that most of the key reasons can be termed “soft issues” which is management parlance for Human Resource issues like cultural differences, mismatch of leadership vision, differences in remuneration structuring and Human Resource policies. An acclaimed McKinsey study on mergers stated that the overwhelming reason was “something loosely called culture”. When it comes to culture, employee communication and other so-called ‘soft issues’, the Human Resource function has a role to play in making the M&A activity successful. Most experts believe that getting Human Resource involved at the very beginning of an M&A decision would help employees deal with the culture shock post merger or acquisition.
This research paper examines the role of Human Resource function, seeks to unveil the Human Resource-related reasons for M&A failures, find ways and means which could help Human Resource Managers to make the “marriage successful”.

KEYWORDS: Acquisitions, Cultural Alignment, Due Diligence, Human Resource, Mergers.

INTRODUCTION
In recent decades, M&A’s have increasingly become the preferred method of expansion, much ahead of organic growth. However, getting the HR issues right will be critical to any deal’s success. An acquirer must understand the target company’s workforce and the factors that will affect its integration. Care should be taken to uncover differences in how staff are motivated and rewarded, especially when their employer’s strategic priorities change because of the deal. The HR and broader people issues of an M&A deal are commonly cited reasons why deals fail.

MERGERS AND ACQUISITIONS
Mergers and acquisitions represent the end of the continuum of options companies have in combining with each other. With our focus on mergers and acquisitions, it is important to distinguish them. In a merger, two companies come together and create a new entity. In an acquisition, one company buys another one and manages it consistent with the acquirer’s needs.

REASONS FOR M&A’S
There are numerous reasons for companies to merge or acquire. Some of the most frequent include:

- Horizontal mergers for market dominance; economies of scale.
- Vertical mergers for channel control.
- Hybrid mergers for risk spreading, cost cutting, synergies, defensive drivers.
- Survival & Growth for world-class leadership and global reach.
- Financial gain and personal power.
- Gaining a core competence to do more combinations.

ASSUMPTIONS
Regardless of the reasons companies have for merging or combining, there are several basic assumptions being made, either explicitly or implicitly. These include:

- M&A’s are the fastest and easiest ways to grow.
Creating synergies and Molding cultures is a major challenge.

Soft and hard due diligence are necessary but not sufficient conditions.

Pre-planning can help increase chances for success.

**REASONS FOR FAILURE**

Mergers and acquisitions fail for a variety of reasons, typical reasons for failure include:

- Expectations are unrealistic.
- Financial drain, hastily constructed strategy, poor planning, and unskilled execution.
- Talent is lost or mismanaged.
- Power and politics are the driving forces, rather than productive objectives.
- Culture clashes between the two entities go unchecked.
- Transition management fails.
- Focus of executives is distracted from the core business (Charman, 1999; Sparks, 1999; Doz and Hamel, 1998).

**REASONS FOR SUCCESS**

Perhaps not surprisingly some of the major reasons for success in mergers and acquisitions include:

- Leadership.
- Well-thought out goals and objectives.
- Due diligence on hard and soft issues.
- Well-managed M&A team.
- Planning for combination and solidification steps completed early.
- Key talent retained.
- Extensive and timely communications to all stakeholders.
THE MERGER & ACQUISITION LIFE CYCLE

There are five key phases to the life cycle of mergers and acquisitions. These can be identified as follows:

PRE DEAL (TARGET EVALUATION) - In this early phase the organization defines its objectives and desired outcomes of the merger or acquisition and searches for suitable entities. During this phase it is usual to develop a set of criteria for the selection of a suitable entity. This often involves extensive research and gathering of market intelligence to assess the potential of suitable candidates.

DUE DILIGENCE - Once a suitable entity has been identified, usually the next step is to make an offer to acquire or merge with the new entity. This offer is usually made conditional on the completion of a due diligence. During this second phase, a review of the new entity is undertaken to ensure the soundness of the deal and to assess any risks involved with the completion of the deal. Often many transactions do not go beyond this phase because the due diligence highlights the inappropriate risks associated with the deal.

INTEGRATION PLANNING - In this third phase detailed plans, milestones and activities are developed to ensure the successful implementation of the deal. This phase is often conducted under very tight time frames and requires extensive and detailed involvement from experienced personnel. Detailed project management plans are established to ensure the smooth implementation of the deal.

IMPLEMENT MERGER - Phase four requires the execution of the detailed planning conducted in phase three. Again, this phase is usually conducted under tight time frames and requires the execution of many complex plans simultaneously. Strong project management skills are required during this phase. The implementation phase is very visible to shareholders, staff, clients and competitors and is conducted under tremendous scrutiny of these parties.
EVALUATE MERGER - The final phase requires reviewing the performance of the new entity to ensure that a successful integration has been completed and that the objectives of the merger or acquisition have been achieved. Performance of the new entity is assessed against the original objectives determined in the Pre Deal phase.

ROLE OF HR IN DIFFERENT PHASES OF M&A LIFE CYCLE

THE ROLE OF HR IN THE PRE DEAL PHASE

Typically in Asia, there is little involvement of HR professionals in the first phase of mergers and acquisitions. However, there is a critical need for HR to be involved in this phase. One of the first critical areas that HR can be involved is in assessing the potential compatibility of cultures. This involvement could also extend into phase two of the process as part of the due diligence. This could involve reviewing an array of things such as leadership style, mission, vision and values of the organization, team strength, performance and reward management systems, customer focus and organizational capabilities. One of the challenges that HR faces is obtaining this information in an environment where the organization may not want to alert other parties of their intent to acquire or merge. As such, much of this information is usually obtained on an informal level or through the use of third parties.

THE ROLE OF HR IN THE DUE DILIGENCE PHASE

During this phase, the organization determines the associated risks and the soundness of the deal. It is at this stage that the organization determines whether it will purchase the entity and its correct value. Many of the HR activities identified in the pre deal phase are continued with greater detail in the due diligence phase to ascertain the correctness of the perceptions obtained in phase one. It is during the due diligence phase that potential problems and risks are often identified. It is particularly important that the HR representatives access professional help when dealing with acquisitions in countries outside of their own areas of expertise and knowledge. During this phase it is important to determine any liabilities that may be a result of partial or unfunded benefits such as retirement schemes, long service leave and other accrued benefits.

THE ROLE OF HR DURING THE INTEGRATION PLANNING

HR is usually involved in a wide range of planning issues such as:

• Talent management and retention initiatives for key personnel;
• Determining transition strategies to move people to new roles, provide training and reskilling;
• Determining the leadership style and new management team for the new set up;
• Determining the direction for the new organizational culture;
• Designing the communication strategy for staff;
• Appointment criteria for new positions and development of the contract terms of employment for the new entity;
THE ROLE OF HR DURING THE IMPLEMENTATION PHASE

Effectively, during the implementation phase, HR is required to deliver on the plans developed during the integration planning phase as well as respond to unexpected and new requirements – which are often many and unpredictable. One of the key roles for HR professionals during the implementation phase is the co-ordination of communications to staff. It is critical that the new organization maximize productivity and focus on client and shareholder satisfaction as soon as possible. HR can play a pivotal role in maximizing employee engagement through effective and timely communications to staff. As well as the important role of implementing the employee communication programme, there are several other activities typically conducted by HR professionals during the implementation phase. These include:

• Acting quickly to restructure the organization and select the right people for each role including people management, assessment and development;

• Aligning business strategies with people practices;

• Establishing financial and legal liabilities and compliance management;

• Managing cultural and organizational change;

• Issuing new employment contracts with revised terms and conditions;

• Developing and harmonizing HR policies and programmes across the group;

• Assisting in organization and process redesign;

THE ROLE OF HR IN EVALUATING THE MERGER

It is often tempting for management to get caught up in the excitement of searching for and acquiring new business opportunities. An important phase in the merger and acquisition cycle is the post merger phase when a review of the achievements of the merger can be assessed against the original or revised objectives. The failure rate for successful mergers is high at around 70%.(Source: Gaplin and Hendron). It is important for the management team to review the progress and success of the implementation phase.

EXHIBIT 1:“EVIDENCE SUGGESTS THAT INVOLVING HR IN A SIGNIFICANT ROLE EARLIER IN AN ACQUISITION MAKES SENSE.”
THE HUMAN SIDE OF M&A ACTIVITY

Plenty of attention is paid to the legal, financial, and operational elements of mergers and acquisitions. But executives who have been through the merger process now recognize that in today’s economy, the management of the human side of change is the real key to maximizing the value of a deal. HR's role in mergers and acquisitions is crucial to increase chances of a successful deal. Employment law challenges, culture clashes, talent retention and employee engagement are all potential pitfalls that can be avoided through the HR team playing a significant role in the end to end M&A process.

MAJOR HR ISSUES IN MERGERS & ACQUISITIONS

Let’s look at the HR issues that inevitably arise in mergers and acquisitions.

LACK OF COMMUNICATION: Lack of communication during mergers and acquisitions has long been identified as the most critical need. As we examine the HR issues involved, we will see a lot of references to the fact that people resist mergers, acquisitions, and especially takeovers at a personal level. The reason why they resist at a personal level is because they have not been told why things must change or how they are going to change.
LACK OF TRAINING: As companies merge and acquire one another, they tend to merge technologies. They also merge policies, processes, and procedures. In a merger situation, approximately 50% of the people do not know the new software, policies, processes, and procedures. If proper training is not imparted to those people, it will end up being negative influence on the outcome.

LOSS OF KEY PEOPLE: Good people – key people – tend to leave organizations at this particular point in time. Many people are afraid of losing their jobs. It is a well-known fact in the business world that mergers and acquisitions usually cause staff reductions and it is true. People who are talented – the exact kind of people whom the acquiring company wants to retain in the organization – are exactly the kind of people who are going to put their resumes out and probably go to some other organization. That is a tremendous loss for an acquiring organization.

CORPORATE CULTURE CLASH: M&A’s success or failure is based on how well the process of “integration of cultures” is undertaken and the HR function has a key role to play here in understanding cultural nuances. These cultural differences could be from a very small issue like, how do you address your peers and superiors, religious sentiments, working hours, dress code, meetings etc.

INCORRECT PEOPLE ALIGNMENT: Statistics have shown that 70 percent of all acquisitions were not able to achieve the desired results for which the M&A happened and the prime reason for this that people aspect has not been given adequate attention. One must realize that it is most difficult to deal with people alignment during any acquisition. Hence, the foremost objective should be to get the right kind of people alignment. It is not easy to achieve the right people alignment because with every M&A comes fear, which can at times become a serious threat to the success of any deal. “The main concern at this point is how to replace fear with hope for those who are acquired.”

HR BEST PRACTICES FOR MERGERS & ACQUISITIONS

Following are the set of high level Best Practices for the HR people when they face the daunting task of managing the complex issues involved in mergers and acquisitions.

LEADERSHIP: That leadership determines outcome of M&A is no exaggeration. While leaders who dare to walk the talk can make this marriage successful, if not, may lead it to divorce. The one thing the organization does not want to do is create a leadership vacuum. HR has to play a pivotal role to identify who those leaders are going to be and they must identify them quickly. Also the HR has to work as a coach and assist the senior leadership in creating the culture. So, HR is the leader of leaders and should teach them the magic of co-leadership where “one plus one is equal to eleven”. This will avoid power struggles and make them jointly fight competition.

INTEGRATION: The integration of two organizations is often the real-world test of a successful merger or acquisition. For the newly combined company, it can mean the difference between ongoing financial success and eventual failure. HR must play a prominent role in any integration team. Integration is fast becoming a specialty discipline within the HR profession. The integration team forms the backbone of the entire effort, and great care must be taken to recruit the best players from all the right functions and business units.
DUE DILIGENCE: For any successful negotiation, and clear cut decisions, the HR team has to conduct due diligence rigorously, ensuring that it is about fact-finding and not evaluation. The team has to look into organizational culture, employment contracts, health and retirement benefits, executive compensation, talent base, retention risks, country-specific regulatory issues, HR operations, and identification of possible redundancies.

BRIDGE BUILDING EXERCISE: To orchestrate a successful deal, HR is an important bridge between the two partners. The three dimensions of an acquisition are the strategic, financial and cultural fit. Cultural alignment; channeling participants to a shared common vision; empowering the right managerial talent, and addressing organizational uncertainties are values dear that make a successful deal.

TIMING OF COMMUNICATION: The timing of communication to employees is crucial. Raising the merger too early with employees is likely to generate uncertainty, confusion and worry. At the same time, organizations do not want to let employees know too late, ruling out the possibility of getting some feedback. HR should let employees’ representatives know quite early on about the possibility of merging, but ensuring that these representatives are discrete and are given this information in confidence.

NEW COMPENSATION PLAN: In M&A activity, HR should chart out a new compensation plan as interests of both the companies have to be considered. It is also important as it can make the employee jump ships and look for new job, thereby making a company lose on intellectual capital. The task is all the more painstaking and challenging, inevitably call for a robust and accountable HR team.

RETAINING PIVOTAL TALENT: Talent is generally a key piece of the M&A strategy. HR plays an important role in assessing the talent that is critical to the integration and ongoing success of the entity as many M&A’s have failed miserably due to losing out on the best employees. Retention of key talent from both the companies helps in harnessing the skills of the champion performers to bring out a stronger business. Talent retention during M&A also become crucial as the right talent can save the organization and take it to glorious success.

ROLE OF COMMUNICATION: Prolific and effective communication is the key to any M&A effort. HR plays an important role in spreading the word. What required at this point is continuous, honest and open communication. Most of the employees fall prey to grapevines. HR must play a vital role in creating a transparent organization and communication channels must remain open.

UNDERSTANDING AND ALIGNING SEPARATE CULTURES: It is seen that most of the M&A’s fail because of the cultural issues. One of the major challenges for the HR is to educate the employees about the culture of the new organization. It can also play an important role in helping to understand cross-cultural sensitivities and integration challenges, which today are prime elements determining the success or failure of any M&A.

ACCESSIBILITY: HR can be a true help desk by being accessible any time, anywhere, and be well prepared to answer inquiries by employees from the company being acquired as well as the
acquiring company. Any information or guidance that can be provided to employees at any level to address uncertainty is of critical value.

EXHIBIT 2: “HOW EFFECTIVELY HR SUPPORTS THE ORGANIZATION IN SUCCESSFUL V/S LESS SUCCESSFUL DEALS.”

Source: TOWERS WATSON PULSE SURVEY PUBLISHED IN 2009

Sri Krishna International Research & Educational Consortium
http://www.skirec.com
CONCLUSION

If a merger or an acquisition is a success, it creates history, and if it fails, one often reads about it in the management books as a case study. It is believed that M&A’s are substantial financial events that are trusted to enhance long-term profitability of an expanding organization. In such a scenario, it becomes important to identify the champions or key talent of the organization, and thus, one has to measure the performance to separate the grain from the chaff. As mentioned earlier, an M&A is like a marriage alliance. Just like the mere exchange of vows does not guarantee marital success, the mere signing of documents does not ensure the success of an acquisition. It is the quality of ‘experience’ and the new relationship which seals longevity and productivity. As rightly said by Prof. David Heckman, University of Pennsylvania, “HR has a role of a juggler, balancing a number of ‘needs of the hour’ during an M&A. The most critical role it plays is that of being a people’s person in the truest of sense, and lending an ear to the employees for transparent working as well as smooth functioning of the organization”. Our discussions, too, led us to some interesting findings. Foremost among them was the need for HR to be roped in during the initial deal discussions. It is only when the HR team understands the mechanics of the equation can it ponder over the likely people-related worries, and come up with solutions to fit the context of the task at hand. This participation in due diligence will make HR a more effective business partner, as well as proactively identify the areas in which it can make an impact. In the words of Mr. Sanjay Sinha, EVP – M & A (HR) & New Initiatives, Hinduja Global Solutions Ltd. “The biggest risk in any acquisition is the possible lack of cultural compatibility that can lead to “us” versus “them” attitude. Then, there is a constant fear of the unknown, especially among the employees of the target company. The HR team should target the three inhibitors of a deal – Reluctance, Resentment and Resistance”.

When I set out to work on this research paper, my hypothesis was that HR needs to prove itself as a worthy member of the team that heads the gamut of M&A processes. Though much work is already being done in progressive organizations in this regard, there are others where HR still lacks the skills to make a fruitful contribution. Whatever be the degree of value added, research has proved the vital role that HR needs to play in the success of a merger or an acquisition. A 2010 study by Towers Watson has listed the five factors that can make a deal successful: HR performance; better due diligence (financial impact of people-related risks); cultural alignment; focus on success differentiators (key talent retention, change management, workforce deployment and leadership alignment); and, M&A readiness.

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