UNIVERSITY of HOUSTON CBA COLLEGE of BUSINESS ADMINISTRATION

ISRC *Notes* - February 1999

Managing on Shifting Terrain: Mergers, Acquisitions, Alliances and IT

Based on a presentation by Gary Richardson, James McKeen & Gary Moore

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The February ISRC seminar covered the very hot and timely topic of mergers, acquisitions and information technology. Many of our Member firms have had or are having personal experiences with both sides of mergers. Gary Richardson, CIO of Service Corporation International, and Gary Moore, CIO of Telus Corporation, both shared their hands-on experiences with several mergers in which they have been involved. James McKeen, Professor of MIS at Queen's University, led a discussion drawing out the experiences of the seminar participants. The link to last month's ISRC roundtable discussion on managing projects and managing change made these experiences even more meaningful.

Introduction and Overview

The worldwide merger activity for 1998 totaled $2.5 trillion. Every year since 1995 has set a record for mergers. The deals are also getting larger. Mergers over $1 billion dollars averaged $3.2 billion in 1997 and were up to $5.95 billion in 1998. Nine of the ten largest mergers in history occurred or were announced in 1998. The motivations and environmental drivers behind these mergers, including globalization, deregulation, horizontal/vertical integration, are not changing so the trend towards consolidation is expected to continue. Although the promise of savings from synergy has failed to materialize as hoped for.

The problem is that only the IT professional is concerned about the impact of a merger on two (or even more) pre-existing IT organizations. IT issues seem to be below the radar screen as most merger deals are put together. Top management "deal makers" simply are oblivious to or ignore the IT problem and assume that it will get taken care of. The IT management is left to pick up the pieces after the deal is done. IT is on their own trying to address the issues of:

- How can we save money by eliminating duplicated systems and still deliver value?
- Will the existing IT roadmaps serve the strategic goals of the new organization?
- How do we bind the new organization together?

Voices of Experience

Gary Richardson reflected on his personal experiences going through the Texaco/Aramco (Star Enterprise) joint venture formation and then to face it all over again in the three-way joint venture of Texaco/Aramco/Shell. In his new position with Service Corporation International (SCI), acquisition is an almost daily event. Dr. Richardson drove home the point that a governance philosophy needed to come from the top very early in the merger process. Lines of authority and responsibility need to be clearly set and understood before any IT decisions can be made. This gets particularly confusing when there is a merging of equals rather than a "winner" and a "loser".

Gary outlined four different models of migration as follows:

1. Leave each entity's systems and organization alone.
   This hands-off approach is most applicable to mergers between companies in dissimilar businesses. It could also be used as an interim step. Data mapping is a problem, but outputs from each entity can be consolidated in a data mart for management reporting purposes thereby giving the appearance of integrated systems.

2. The big bang.
   In the big bang model one merger partner totally takes over all IT functions from the other partner. Unfortunately this introduces early chaos and does not immediately reflect the cost savings management was counting on. Gary referred to the costs as a bubble that initially increases during conversion of the applications and absorption of the merged entity before finally producing some cost savings.

3. Everyone move to a new internal system.
   In this model a new system is developed/purchased replacing preexisting systems in both merging entities. However, this approach results in the highest cost, greatest change to the organization and highest stress.

4. Outsource the system/function.
   Outsourcing is always an option and maybe a merger is an opportune time to make this kind of a change. On the other hand, the governance issues mentioned earlier become even more critical when you add this other level of control and responsibility for vendor administration.

Whichever approach is chosen it is important to get the governance model right. It is important to clearly define roles and responsibilities. Then a serious team building effort can begin. Internal IT issues should stress clarity and formality. The IT plan should be formalized and should be as *win-win* oriented as possible. This is particularly important because it is very easy to lose your best and brightest during a merger. The more hostile, confusing the environment, the more likely people will seek other opportunities. A formalized tactical plan for implementation must be developed if the merged organization is adopting one of the integration oriented migration models. In addition a working technical standards group needs to determine development and database strategies and a time-phased infrastructure plan.

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Gary concluded by listing his critical success factors.

- Top executive level approval of the IT strategy
- Clear, empowered leader/governance
- Published formal migration plan
- A commitment of resources to the plan
- Emphasis on active team building
- Establish data migration skills and use a data warehousing concept to bridge the gap to integrated systems
- Exercise fully your change management skills (not everyone is happy)
- Deal with the organization cultures and communication

Gary Moore's life experiences echoed many of the same lessons. Dr. Moore's employers have been acquired by other companies, in another situation his company was the acquiring company, and he is now involved with a merger of equals. Each of these mergers/acquisitions involved a different model for migration.

In the first case, which was an acquisition of Gary's company by another, they followed the big bang model that involved retaining none of the acquired company's systems or personnel. The second case involved Mr. Moore's company being the acquiring company but followed a model of "gentle persuasion" wherein the acquired company gradually adopted the systems and procedures of the acquiring company. The third and current merger that Gary Moore is involved in is considered a "merger of two equals". This merger is between Telus and BCTel, two large Canadian telecommunications companies.

The merger was described in detail and clearly reflected the pitfalls involved in these complex combinations. The cultural differences between the two companies and their IT departments are significant. One company primarily outsourced and was a decentralized organization with no CIO. The other had leadership and was centralized with only selective outsourcing. One had operated primarily as a subsidiary of GTE and the other had always been independent. Perhaps the most significant problem will be in the personnel decisions that are being made. The merged companies are trying to the limits to maintain the "merger-of-equals" notion and are assigning personnel to positions so that the 50-50 ratio is retained.

This merger also very clearly demonstrates the problem with the lack of inclusion of IT professionals in the merger activity. The CEO of the merged companies announced to the press that there would be substantial savings from combining IT organizations. But, as Gary pointed out, no one from IT was consulted about the viability of these savings prior to the public announcement.

<u>Open Discussion:</u>

Dr. James McKeen used the analogy of a merger/acquisition from the IT perspective as an "arranged marriage". You are standing at the altar, the vows are being read, and you get a queasy feeling in your stomach. The open discussion was organized under seven questions, which provide a useful framework for developing a migration model appropriate to the particular situation.

1) How do you develop a single vision for IT in the merged organization?
   Each organization has pre-existing visions appropriate for their pre-merger environment. Many mergers result in significantly different strategies for the new organization thereby causing the old plans to be misaligned. The starting point to develop the new IT vision is to first determine the new vision for the organization. The next important step is to determine who is in charge. You must know the governance philosophy and areas of responsibility. Top management must be sensitized to the significance of accomplishing these two steps as early as possible in the merger process. Often it is desirable to develop multiple plans under different scenarios relating to alternative business visions. When the waters become calmer, the appropriate plan can then be presented.

2) How should IT handle uncertainty, retention, communication, and other HR issues?
   The human side of a merger should be addressed first. The key core people should be locked in immediately. It may be that they will subsequently be eliminated but you don't want to lose any at this time. The knowledge they control is critical to any systems migration plan work. Communication within IT must be consistent, open, and factual. There is a lot of misinformation floating around at this time. Rumors spread and people become uncomfortable. If the human problems are under control, the humans will be able to handle the technical problems.

3) What should be done about integrating systems and data?
   There are multiple levels to address these problems. First are the Band-Aids to take care of business-as-usual. Then the planning for integration begins. One suggestion was to draw an integrated total systems architecture picture without specifying which company's system would be used and which replaced thereby avoiding the ownership problems until later. Another interim suggestion was to use a datamart, which can integrate system, outputs and give the appearance of an integrated system.

4) How can we effectively plan and coordinate all aspects of the change?
   Again, the primary concern should be directed towards the people issues. Consistent, honest communication is the cornerstone to success. It is hard enough for IT management to get good answers during these times, the lower levels have an even more difficult job. Some changes may have to be forced,

but if the various challenges can be clearly defined and communicated a teamwork solution can be found.

5) What are IT's roles before and after the merger?
IT management should make top management aware, long before mergers are planned, that there are significant IT problems associated with these business combinations. Hopefully, management would then include IT in the merger process/decision making at an earlier stage. As a minimum management must be made aware that things are not as simple as they may seem and promises of substantial cost savings from synergies may not be immediately realizable.

6) How should existing development projects be handled?
One participant reminded us that sometimes determining what the existing projects are is problem enough. Obviously the disruption of current projects will cause havoc but until the post-merger plans are known, continued development could be wasted effort. Categorizing projects by ignore, wait, kill, address and then applying the appropriate level of response was suggested.

7) What factors should be addressed in integrating cultures?
The issue of cultures was discussed by all the speakers and is obviously one of the most difficult problems to handle. The first step is to just learn each other's languages. Everyone has their own terms or acronyms and these are barriers to communication and integration. The surviving culture should be the one that supports the post-merger IT vision. Changing the culture is an exercise in team building and will require good communication channels and lines of authority. Changing the culture starts with changing/eliminating the opinion leaders. It is also important to have an effective exit strategy for those employees not retained.

<u>Summary:</u>

Mergers, acquisitions, and alliances happen for business reasons such as globalization, vertical alignment, horizontal alignment, access to new markets, synergies of scale, etc. Unless access to IT is a part of the business motivation, top management typically does not include the IT professionals in the pre-acquisition planning. Management just leaves IT to make-it-happen on their own. Unfortunately, subsequent to the merger decision Management often uses savings in IT costs as a justification for the merger but without really knowing where it will come from.

Merger activity is at an all time high and the driving forces point toward the trend continuing. There may never be an ideal time for the impact of a merger to occur on an IT organization and they will often happen with little advanced warning. The models of migration presented by the speakers and participants are a good start to surviving but they still need refinement before we can make this "arranged marriage" work.

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For Additional Information:

http://www.computerworld.com/
Computerworld magazine has several articles on merger activity from IT perspective

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