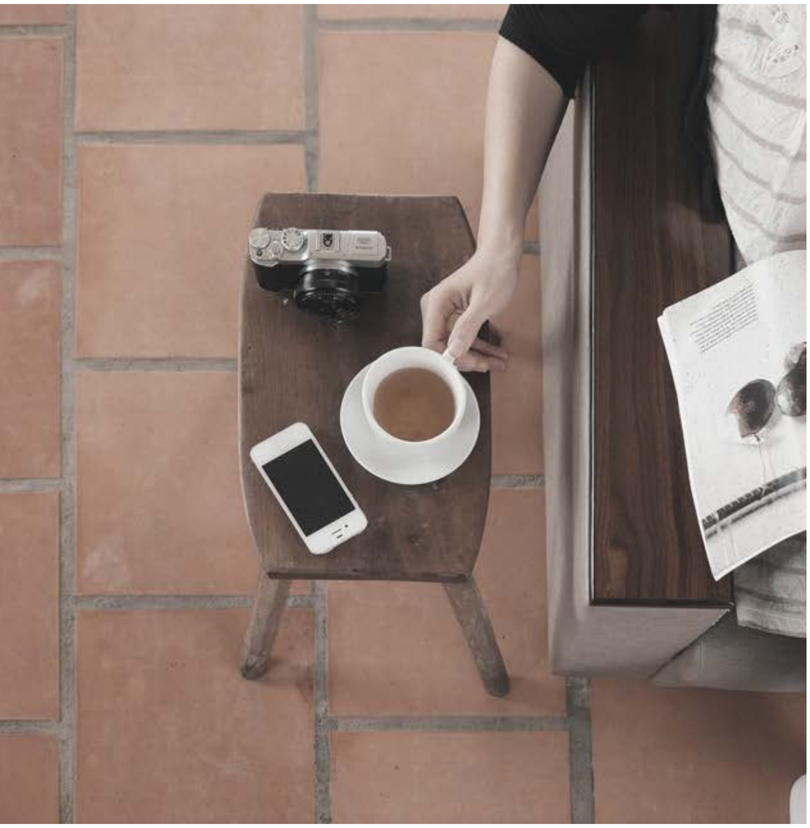
Overcoming the Cultural Challenges in M&A Deals: Know What Your Employees Think Before Shaking Hands

Numerous studies indicate that many merger and acquisition (M&A) deals fail to meet financial expectations – a figure that can vary from 50% to as high as 90%. According to McKinsey research [1], 70% of mergers do not achieve their expected "revenue synergies."

Why do M&As fail? One author suggests a number of pitfalls [2] that can thwart success, one of which involves assigning the chief financial officer or general counsel to act as the "M&A champion." Such individuals, already overwhelmed by the responsibilities of their demanding positions, may not have the time to do a proper job of due diligence. Other underlying reasons for failure or lackluster performance [3] include overpaying for the deal, lacking strategic clarity, making slow decisions, implementing poor integration planning and execution, eroding business fundamentals, allowing competitors to steal customers and market share, and losing key talent. And yet, in spite of that last factor being a reason for failure, talent acquisition – as the rationale for a deal – has more than doubled in importance, rising from 4% to 9%, since the spring of 2016 [4].

Leadership often views talent – one of the key ingredients in any successful enterprise – as a "soft issue" when it comes to business deals. And yet, cultural integration of merging organisations – their missions, values, goals, and workforce – remains as one of the top challenges. Despite the goodwill of both parties, many deal makers misread their own and the new company's culture, unaware of the true nature of their employees. With this lack of knowledge, they falsely believe that the two cultures will fit together seamlessly after a brief interval of time.

Traditionally, to gain knowledge and accurate facts, the M&A team performs extensive due diligence on a potential technology, service, or product to evaluate essential factors (such as financial records), along with anything else deemed material. Yet, unfortunately, insufficient rigor goes into assessing cultural alignment despite the fact that culture assessment and alignment, leadership assessment, talent retention, benefits, and compensation are part and parcel of the due diligence process. Such factors often undergo a superficial evaluation.



Adding to the problem, it is not uncommon for decision makers to depend on both companies' senior management perspectives and assumptions when it comes to cultural issues, often falling short of any objective factual observation on the matter. Or, at the very best, they try to gain organisational insights into each other by tackling observable, tangible matters, such as [5]:

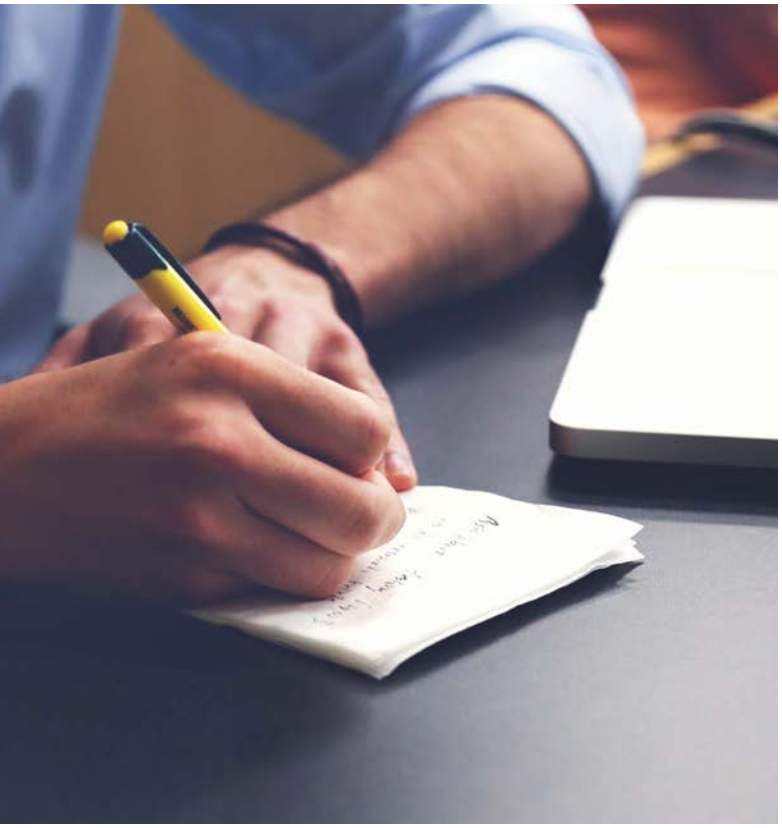
- Organisation development: functional and reporting relationship charts
- Employee relations: potential disputes; employment agreements with officers, directors, key employees, criminal proceedings or significant civil litigation involvement of key employees and officers, and appropriateness of the company's treatment of personnel
- Compensation: pay schedules to officers, directors, and key employees; management incentive or bonus plans; deferred compensation
- Benefits: health, medical, life, retirement, severance or termination pay, vacation, and sick leave
- Administration: employment manuals and policies
- Merger-related items: retention arrangements with key employees, and layoffs and resultant severance costs

As such, however, they totally disregard the need to gain true insights through a deeper understanding of company culture – a deeper comprehension of what makes their organisation function.

"Hard" Approaches Can Make the Difference

The bottom line is that information – about employee desires, goals, commitment and alignment to the company – is critical and, sadly, often lacking. New approaches and tools are a positive way to support informed decision making and shed more light into gaining a more accurate assessment of company culture.

Technology and common sense together can help leadership overcome many cultural issues through the use of better, more accurate assessment tools.

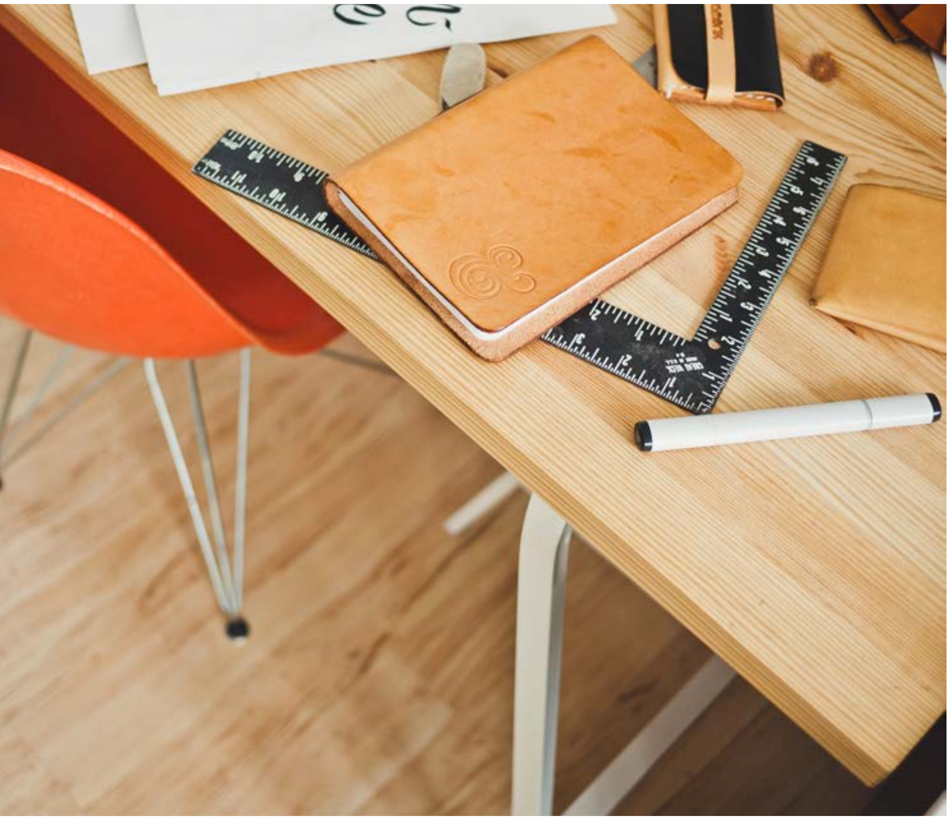


Part of the dilemma in considering new methods is that due diligence on people issues typically focuses on top and senior management perspectives, especially in determining how senior managers in both organisations will work together or take new roles in the new entity. Little to limited worthy effort is spent on layers below senior management. The downside in taking this approach is the assumption that leadership has a clear view of the entire organisation, from managers on down to non-exempt employees. In the end, deal makers base their decisions on mere assumptions of a very limited number of people in both parties rather than on the full big picture.

To broaden those assumptions and get to know the workforce, new approaches and tools can help objectively assess cultural fit or alignment, rather than having deal makers depend on anecdotal or self-biased perspectives. With costly efforts made to uncover the facts about a product, service, or technology, how can managers not do the same for their workforce? When one thinks about the high stakes involved in any M&A deal, financial and human, it is imperative to expend a greater effort to assess the whole organisation. Without a viable and objective assessment of facts at hand when making people decisions, leadership faces an enormous risk for failure, accompanied by wasted time, resources, finances, and human talent.

And the waste can be significant. With no coordinated retention actions taken, for example, one study found that 47% of all senior managers in an acquired firm leave within the first year [6]. Beyond that, within the first three years, 72% are on their way out as well. Added to this cost are other factors: employees who remain but underperform, having lost commitment to their job or organisation. To retain valuable talent and minimise such appalling losses, deal makers should recognise that employees need to feel secure and important, be able to provide input, have control over options, understand the "why" of the merger and their place in the new structure.

It does not make sense to discuss whether two company cultures are compatible before even knowing what these two cultures represent. In addition, as company culture is such a broad term, it makes absolutely no sense to refer to it as a singular carved-in-stone definition.



There are almost as many cultures as there are employees in any organisation. Therefore, there is no point of talking about culture compatibility if one does not truly understand one's existing culture and workforce.

Extra Effort Minimises the Risk of Failure

The problem may simply be that cultural challenges are considered "soft" issues that do not have "hard" answers. After all, soft issues fall into the intangible realm, poised to be shaped in any way people want them to be. And that is the moment that logic is lost and deal makers deviate from an effective decision-making process.

However, it does not have to be this way. Technology and common sense together can help leadership overcome many cultural issues through the use of better, more accurate assessment tools. Gaining a deeper understanding of people's true aspirations and aligning that with the new company's strategic priorities is a much more powerful approach than just basing decisions on a handful of people who have an approximate and self-biased approach to cultural assessment.

[1] Cited by Neil Hodge, "Why Do M&As Fail?", Risk Management Magazine (April 3, 2017).

[2] Marvin Dumon, "8 Reasons M&A Deals Fall Through," Investopedia.com

[3] "How 'Good" Deals Go Bad: The Most Common Causes of M&A Failures," Mergerintegration.com

[4] "The State of the Deal: M&A Trends 2018," Deloitte

[5] Richard D. Harroch and David A. Lipkin, "20 Key Due Diligence Activities in a Merger and Acquisition Transaction," Forbes.com (December 19, 2014)

[6] "How to retain Key Talent in an Acquisition," Mergerintegration.com

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