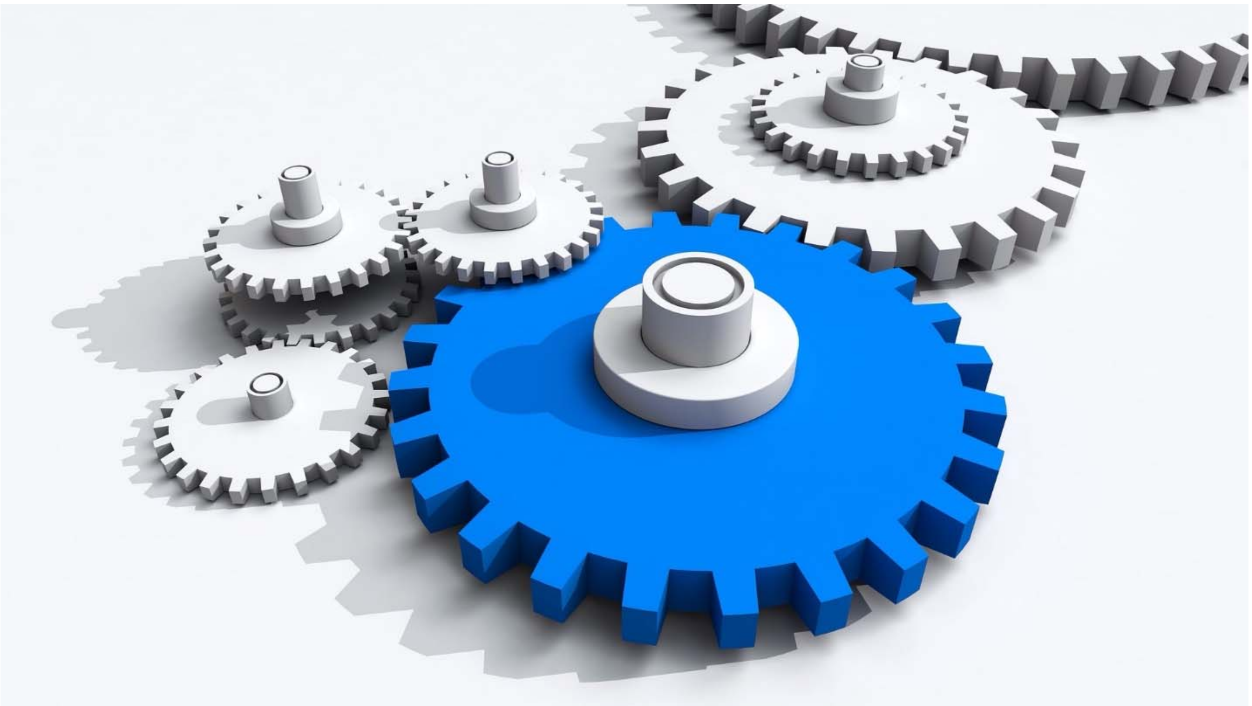

POST ACQUISITION INTEGRATION- FIRST 90 DAYS *by Esteban De Bernardis*

Prior to the completion of a deal, a comprehensive due diligence is required to help the buyer understand critical areas that could have significant impact for the acquired business during the first 90 days of operation under new ownership. The due diligence process should cover operations, finance, legal, HR, tax, and occupational health and safety, as well as any other functions that may be critical for the specific business.

Some of the critical issues that a buyer would have to deal with during the first 90 days would be dependent on the type of deal (assets vs shares) but the vast majority of issues that may occur are common to both deal structures.

COMMON ISSUES:

The following are some examples of post-completion challenges that would require immediate action during the first 90 days:

- **Employee Retention**: In the professional services industry and under normal circumstances, employee retention is paramount. If the acquired company is not able to retain employees post-completion of the acquisition, the ability of the organization to generate future revenues and thus achieve the anticipated returns in the discounted cash flow would be compromised.

In order to minimize the risk of employees leaving the organization, it is important that senior management clearly communicate not only the strategic intent of the deal, but also what the transaction means for its employees, along with company expectations. Presenting a compelling story around how the acquisition would provide better opportunities for all the employees is a helpful tool for employee retention. In the absence of communication, employees may create their own story.

The buyer needs to remember that a vast majority of acquisitions fail to deliver expected returns, and that more than 50% of those failures are attributed to cultural differences that are not properly identified during the due diligence process or addressed during the integration process. Culture is obviously critical in cross borders transactions but equally important when two organizations operate under different sets of values and culture despite being in the same region. Based on my global M&A experience, cultural differences are the most important issues to address and it starts with the identification process during due diligence. It requires significant effort during the first 90 days and beyond, and reinforcing activities such as team building exercises remains a critical component of the integration process.

- **Working Capital**: The Share Purchase Agreement (SPA) or Asset Purchase Agreement (APA) most likely included a formula with a target working capital to prevent working capital from being transferred out of the organization prior to the divestiture. The target working capital is normally calculated as a historical average during a certain period of time, normally a year. Depending on the seasonality of the business, the date of completion, and the strategic plans post-completion, the level of working capital may not be enough to finance the business in the short-term. Employee salaries, vendor invoices, and taxes may be due shortly after completion. Additional working capital may be required and it is important to identify this need in advance. In fact, it should be captured in the Discounted Cash Flow model used to calculate the Net Present Value (NPV) and Internal Rate of Return (IRR).

  Depending on cost savings synergies and expected revenue growth, additional working capital may also be required in the long term. In my next article I will focus on the longer term initiatives that are a critical part of the integration process.
- **Risk Management**: It is important for the buyer to have an insurance policy in place that covers business arising risks from the day of acquisition. In the case of a shares deal, insurance policies are likely already in place and the due diligence process would indicate if the coverage is sufficient or not according to the buyer's risk tolerance. Based on this, the coverage could be increased, reduced, or cancelled. In the case of an asset deal, it is more complex since it may require an expansion of the buyer's insurance policy to cover the risks of the acquired business. Organizations that are very acquisitive normally have in place a blanket insurance policy that would automatically cover predetermined risks of any acquired company. This reduces the complexities concerning insurance during completion of the deal.

  Another important aspect to consider are pre-existing risks. What if after completion there is a claim for a deficient product or service that was provided before signing the deal, under the previous ownership? Who would be responsible for this claim and the associated risk for directors and officers? A run-off insurance policy would cover this, but it must be purchased by the acquired company prior to the transaction. The term is typically set for several years and the policy is normally not costly. Nevertheless, it should not come as a surprise after purchase price and the terms of the agreement were negotiated to exhaustion.

- **Treasury**: In the case of an asset deal where no legal entity is being transferred, the acquired business will not have bank accounts post transaction. New bank accounts need to be established. Sellers normally agree to transfer bank deposits that after post-completion continue to go to their bank accounts, but new bank accounts would be required in order to pay vendors and salaries.

BEST WAY TO PREPARE:

The buyer should ensure that a proper due diligence process is conducted in order to have clear visibility of the issues at hand. The buyer should be ready to address them early in the integration process. Recommendations to prepare for integration include:

Create a cross functional integration team: The integration team would be responsible for the successful integration between the acquired company and the buyer. This includes all the functions in the organization and is therefore critical that all areas of the business have an owner that is part of the integration team. Normally the integration team would have representation from operations, finance, accounting, information technology, human resources, legal, marketing, and other critical functions.

In order to ensure that the critical information gained during the due diligence process is useful during integration and that the strategic plan is followed, the buyer should make sure that some members that were part of the due diligence process and acquisition teams are also included in the integration team.

Another important aspect to consider in order to make sure that a best practice approach is followed, and a "conquer" approach is avoided, is to include key members from the acquired business on the integration team.

It is best practice to appoint an integration leader who would ultimately be responsible for all the integration activities. The integration team should meet on a regular basis to discuss integration initiatives and to report status and progress made to date to senior management.

In addition, it is important to establish an integration steering committee in order to make sure that both the original strategic plan and rationale behind the acquisition are followed. In a mid-sized organization, this team is normally comprised of C-Level executives or functional leaders. The steering committee would meet with the integration leader and key members of the integration team to receive updates and to make critical decisions.

Create a timeline: In order to keep track of all the initiatives that should take place and the expected timing for completion, it is important to create a Gantt chart highlighting the list of activities and dependencies, along with a projected start and end date for each item. Progress made against this Gantt chart should be reported regularly to the integration team and to the steering committee.

Another useful tool is the creation of a scorecard that reports the integration status for the subcomponents of each function.

It is important to note that it may not be necessary to integrate everything. If the acquired business is vastly different than the buyer's business, and the IT system of the buyer cannot accommodate critical information required to run the new business, a case could be made to make a partial integration for accounting and reporting but leaving the existing IT functionality in place until a definitive solution can be found.

CONCLUSIONS:

An acquisition represents a significant investment of funds and other resources in general. It is recommended that the level of complexities are properly evaluated and expert consultants are hired to provide the necessary support during the different stages.

It is critical to pay attention to cultural differences and address them during several workshops and team-building exercises. As Peter Drucker once said "culture eats strategy for breakfast".

Set up a cross functional team, assign clear responsibilities for the integration process, and monitor progress.

Implementing these recommendations can vastly improve the post-acquisition integration process and ensure a higher success rate of business combinations moving forward.

About the author: Esteban De Bernardis is a C - level Corporate Finance executive who has lived in Canada, Germany and Argentina. He is a Chartered Accountant from Argentina who holds an MBA from Rotman School of Management (University of Toronto) and CM&AA (Certified Mergers and Acquisitions Advisor) designation from the US. He has extensive experience in the M&A field having led mid-sized deals and integrated several businesses in Canada, US, Argentina, Germany, UK, Italy, Taiwan, Japan and South Korea.