

HUMAN CAPITAL RISK IN MERGERS AND ACQUISITIONS



HUMAN CAPITAL RISK IN MERGERS AND ACQUISITIONS: 2012

ACKNOWLEDGEMENTS

We gratefully acknowledge the efforts of our survey respondents and our forum participants who took valuable time away from their day jobs to participate in this work. We are particularly grateful to our research partner, Towers Watson, without whom this study would not have been possible.

A handwritten signature in black ink, appearing to read "Christian Bellavance". The signature is fluid and cursive, with the first name "Christian" written in a larger, more prominent script than the last name "Bellavance".

Christian Bellavance
Vice President, Research and Communications
Financial Executives International Canada

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EXECUTIVE SUMMARY

Most Canadian senior finance executives who participated in a recent survey on mergers and acquisitions say their recent M&A transactions were at least somewhat positive, but only a minority characterize those transactions as true winners.

Only one out of five executives who had been involved in mergers or acquisitions during the past five years, and who responded to a survey by the Canadian Financial Executives Research Foundation (CFERF), said their recent transactions were very successful. This stands in contrast to half the respondents, who were more circumspect, stating that overall, their recent transactions were only fairly successful. (The remainder said their transactions were either not very or not at all successful, or they did not know.)

Although the judgement of the success of the transactions is self-reported by the financial executives, the survey respondents based their answers on the metrics they used to determine the success of their transactions. Seven out of 10 measured revenue growth, and three out of five measured both profit margin growth and specific synergies other than cost reduction. Nearly half included the retention of key talent in their metrics. Therefore, the companies rated their past transactions using quantitative data.

The study also identified a number of key practices used by the most successful companies that organizations may want to consider when embarking upon an M&A project.

Although only a minority of respondents said their recent transactions were very successful, this did not seem to deter survey participants from future attempts. The vast majority (more than 80%) of survey participants said they were at least somewhat likely to do another M&A in the next 24 months. Therefore, the strategies used by the most successful companies are likely to be of interest to all to better the chances of organizations reaching their intended goals. The most successful companies will also be interested to see what they're doing right.

EXECUTIVE SUMMARY

This study, sponsored by Towers Watson, attempts to pinpoint and highlight what these highly successful companies did differently in their M&As from a human capital standpoint. What methods, practices, processes or procedures did they use during due diligence, pre-deal planning and later integration of staff? Both an online survey and an executive round table research forum were used to collect data and insights on human capital risk in M&A from CFOs and other senior finance executives.

The research found that most companies with a recent history of “very successful” transactions shared a set of specific strategies that were different from other respondents.

- 1. Very successful companies used these M&A processes and governance policies:**
 - Identified integration managers
 - Communicated approval authority early in the deal process
 - Updated periodically their internal M&A processes and tools
- 2. During the due diligence review of human capital matters, very successful companies:**
 - Established a timeline of events
 - Sought out specific human capital related synergies
 - Had a summary description of their own cultural attributes
 - Established staffing needs and a selection process
 - Had pre-determined opening positions on how employee programs and policies would be integrated
- 3. During the integration planning stage (pre close, before Day One), very successful companies:**
 - Put a process in place to monitor employee attitude and engagement
 - Had an integration plan template available before Day One (date of deal closure)
 - Had a plan in place to help employees cope with changes
 - Created a planning template or process to address a list of integration issues post closing

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4. During the implementation stage (Day One and beyond), very successful companies:

- Improved access to learning and development opportunities for their employees
- Used communication plans and employee surveys to address cultural differences
- Had mentoring programs in place
- Were less impacted by the loss of key talent or executives
- Used tactics such as frequent communication from leadership to boost employee productivity

Human capital risk stands out as an area that requires attention when an organization enters a period of transition and a mood of uncertainty emerges amongst staff. While it may seem that employees at an acquired company, for example, would feel more uncertain than staff from the acquiring organization, workers from the latter are not immune to apprehension about how the transition will affect them. Companies must therefore be aware of a myriad of potential human capital risks before even entering a due diligence process.

Based on the strategies outlined above, it appears that the companies which were most diligent about planning, using tools such as timelines and planning templates, well before the integration stage, will be best positioned for a successful M&A. It's therefore clear that an early assessment of key factors – including issues such as corporate culture, talent retention, harmonization of compensation, benefits and other programs – must be undertaken during the due diligence stage, not after Day One.

RESEARCH METHODOLOGY AND DEMOGRAPHICS

RESEARCH METHODOLOGY AND DEMOGRAPHICS

Human capital risk in M&A 2012 was prepared by CFERF and sponsored by Towers Watson. It comprises the results of an online survey of executives, which was conducted between February 8 and March 23 of 2012, and was completed by 78 respondents. 72% of respondents worked in finance, while 10% worked in HR, 8% were CEO or COOs, and the rest worked in other departments.

Of the survey participants, 85% were involved in an M&A in the past five years, and 15% were not. Nearly half of all participants had made three or more acquisitions in the last five years. More than eight in 10 said their company was either somewhat or extremely likely to make an acquisition in the next two years. For more demographic information, please see Appendix A.

The results of the online survey were complemented by insights obtained during an executive research forum held in Toronto on March 7, 2012.

M&A PROCESSES AND GOVERNANCE

HUMAN CAPITAL RISKS

Differing leadership styles emerged as the most significant human capital risk affecting the value of transactions. Eight in 10 respondents identified this issue as a leading factor affecting value (Chart 3). The companies with the best track record of successful M&As were most likely to cite leadership style and views as factors affecting the value of their transactions.

An acquired company headed up by a founder or entrepreneur with a significantly different leadership style from the buyer appears to present a challenge. If the acquirer wants to retain the leader for his or her knowledge of

the business, then the acquiring company must work to accommodate and integrate the different leadership style. If the founder's knowledge is not critical to the future of the integrated company, the survey results and the insight gathered at the executive roundtable indicate that the leader of the acquired entity should be transitioned out.

Even if six in 10 survey respondents indicated that the loss of key executive talent was a major factor affecting the value of their recent transactions, it appears that the departure of a leader doesn't necessarily have a negative impact on the retention of key executives. For example, the most successful companies in an M&A were least likely to be impacted by the loss of key talent or executives, indicating that those companies

worked to identify and retain key executives early in the process. (See the due diligence section of this report.)

Differing leadership styles: differing opinions

“We don't buy egos. Egos are expensive. They're difficult to coddle. . . . It's all about how they built the business 20 years ago. And most of them are on earn outs anyway, and they're half asleep on their way out, and they are already thinking about their second career. When we make acquisitions, we make sure the leaders have stars underneath them, and we go right to them. We find that entrepreneurs that want to go, tend to do succession planning. We keep the people that do the work; the people that have attachments to clients.”

Derek Petridis – VP Finance, Shikatani Lacroix Brandesign

“There's a constant over-emphasis on how important some individuals might be from a knowledge base and it's always overestimated. If they're not going to be part of your strategy for the next five years, they need to go as quickly as possible.”

Laurie Tugman – Former Chief Executive Officer, Marsulex Inc.

M&A PROCESSES AND GOVERNANCE

The study found that the problems with integrating staff were also significant or very

significant factors affecting value, including cultural differences (cited by 75% of survey respondents) and differences in compensation levels (43%). Several executives observed that although there may be additional costs to incur harmonization such as benefits and IT systems, it's important that these components be addressed quickly to create a successful, cohesive unit.

“Unless they are at the age where they really want to go play golf, entrepreneurs sit until their non-compete clause is over and very often start a new business in competition with the one they sold. So you might as well get rid of them early on, so that they find some other non-competing business to do versus starting the exact same one when the non-compete is over.”

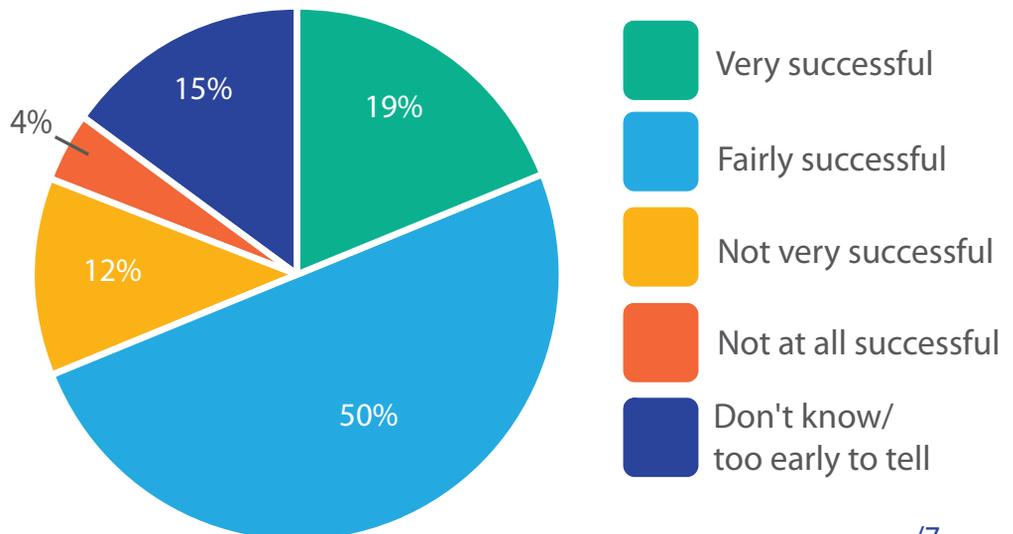
Amit Loomba – Director & Team Leader, Commercial Banking, CIBC

Compensation and benefits

“There's a cost to integration. There are all sorts of costs that you've got to incur and there's a resistance to paying for these, whether it's a change in the accounting system or the benefits plan. The human element, the impact on strategy and culture, for example, are way underestimated in terms of why these elements need to be addressed as quickly as possible.”

Laurie Tugman – Former Chief Executive Officer, Marsulex Inc.

CHART 1: BASED ON THOSE METRICS, HOW SUCCESSFUL HAVE YOUR TRANSACTIONS BEEN OVER THE LAST FIVE YEARS?



HUMAN CAPITAL RISK IN MERGERS AND ACQUISITIONS: 2012

For some companies, it's important to keep the founder as long as possible, even if just for a transition period, to reduce the risk of loss of corporate knowledge and to maintain continuity in leadership. "I've always worked in companies with strong entrepreneurial leaders," notes Bob Rollwagen. "And dealing with this leadership style was a big issue. The rest of it can generally come in hand after that. We never lost a founder of an acquired company because our focus was: We need to get this guy onboard. We can understand his style. We need to figure out where he's going to fit into our leadership

Cultural differences

“Even over short geographical distances, integration can be challenging. With a previous company, we were based in Vancouver and the acquired entity was located on Vancouver Island where it had three or four offices. Integrating the different cultures and processes was difficult. You'd think a small body of water wouldn't make such a difference, but it ended up being significantly challenging. I'd say it was an eye opener for us.”

Brad Cruickshank – Chief Financial Officer, Dueck GM

“What we found with several acquisitions that some people don't understand acceptable conduct, especially if you're dealing with government contracts. We got burned once. Unfortunately it's easier to get a business license than it is to get a dog license. You don't know who the heck you're dealing with sometimes. So you just have to be Very thorough in your due diligence.”

Frank Hunaus – Chief Financial Officer, Ebcu Metal Finishing LP

“In my experience the area where we had the most difficulty was with the culture. You agree on certain things, identify key people, but if the cultural integration is not there, it can be very difficult.”

Carl Gauvreau – President at Gauco Inc. and former CFO, Hartco Inc.

“Sometimes, people leave because they're very demoralized and don't feel engaged anymore. If you haven't kept them informed and part of the process, you've likely lost their engagement and productivity. This translates into a huge risk. One needs to focus not only on the people that you want from the acquired company, but also the key talent you want to retain from within your own organization. It has been my experience, that the lack of attention, particularly, to the all-stars within your own company, has been one of the top reasons why M&As aren't successful.”

Vicki Nishimura – VP Corporate Controller, Prism Medical Ltd

M&A PROCESSES AND GOVERNANCE

team, and then really focus on that, because he will then influence substantially all the other aspects.”

But other finance executives said that they actually encouraged the departures of the founders or CEOs at the companies they acquired, and this for a number of reasons. For instance, they didn’t want to go through the trouble of coddling the entrepreneurial ego, they view founders as expensive to keep around, and feel that these individuals might not be as productive and engaged as they were when they owned the company.

Employee engagement or productivity was seen by 67% of respondents as a significant or very significant factor affecting the value of transactions.

METRICS: DETERMINING SUCCESS

Of the survey participants, 85% were involved in an M&A in the past five years, and 15% were not. Most survey respondents painted at least a somewhat positive picture of their recent transactions. The executives surveyed said the transactions were either fairly successful (50%) or very successful (19%). 16% were not very successful, not at all successful. The remaining companies said they did not know or it was too early to tell. See Chart 2.

“ If it’s not working out, we want to hear it. We want feedback, because we have a people business. We want them to tell us where we failed.”

Derek Petridis – VP Finance, Shikatani Lacroix Brandesign

About one-third of survey respondents measure success metrics six to 12 months after the close of transaction, while another one third do this 12 to 24 months after the close. Very few (8%) begin before six months have passed and similarly, very few (5%) wait 36 months or more.

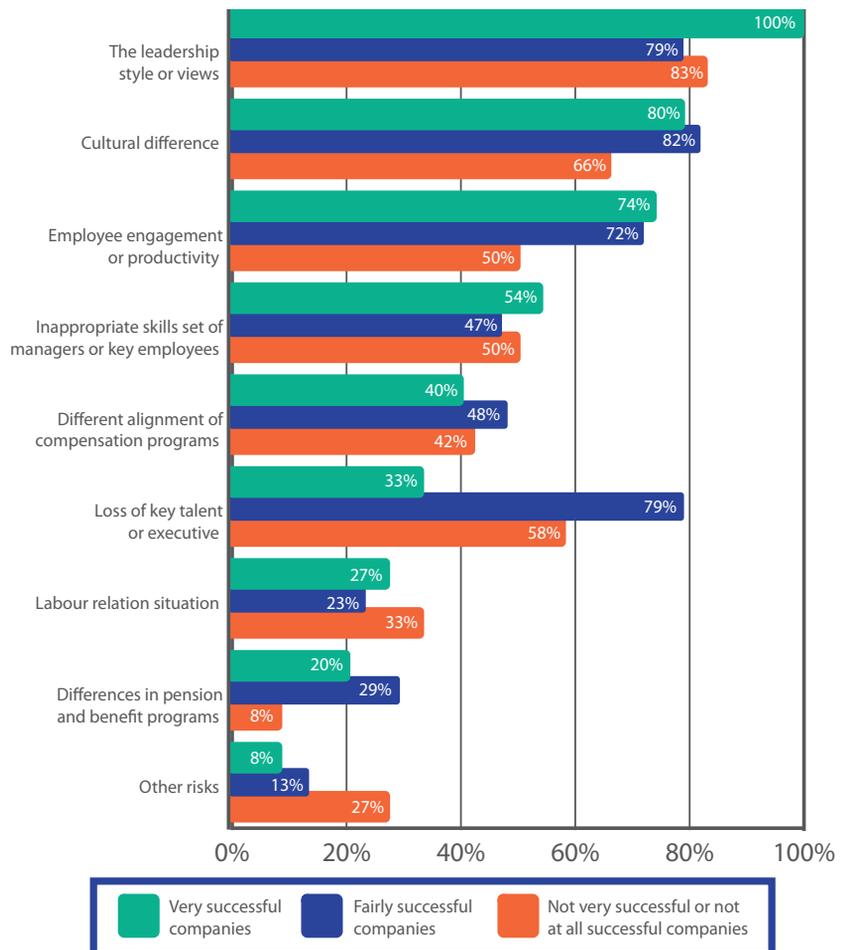
The most common metric used to determine success is revenue growth (69%), followed by the achievement of specific synergies other than cost reductions (63%), followed by profit margin growth (62%). See Chart 3.

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Despite the mixed results with regards to past success, the vast majority (more than 80%) of survey participants were optimistic about future transactions, stating they were at least somewhat likely to do another M&A in the next 24 months.

Finance is often at the helm when it comes to taking the lead on the M&A process. Nearly one-third of respondents said finance had primary responsibility, while 38% said it was the CEO/COO. However, HR was more likely to take the lead on assessing and mitigating the human capital risks (37% mentioned HR first, compared to 26% for the CEO/COO). Only 18% said finance took the lead on assessing and mitigating human capital risks (Chart 3).

CHART 2: HOW DID THE FOLLOWING HUMAN CAPITAL RISKS IMPACT THE VALUE OF YOUR RECENT TRANSACTIONS?

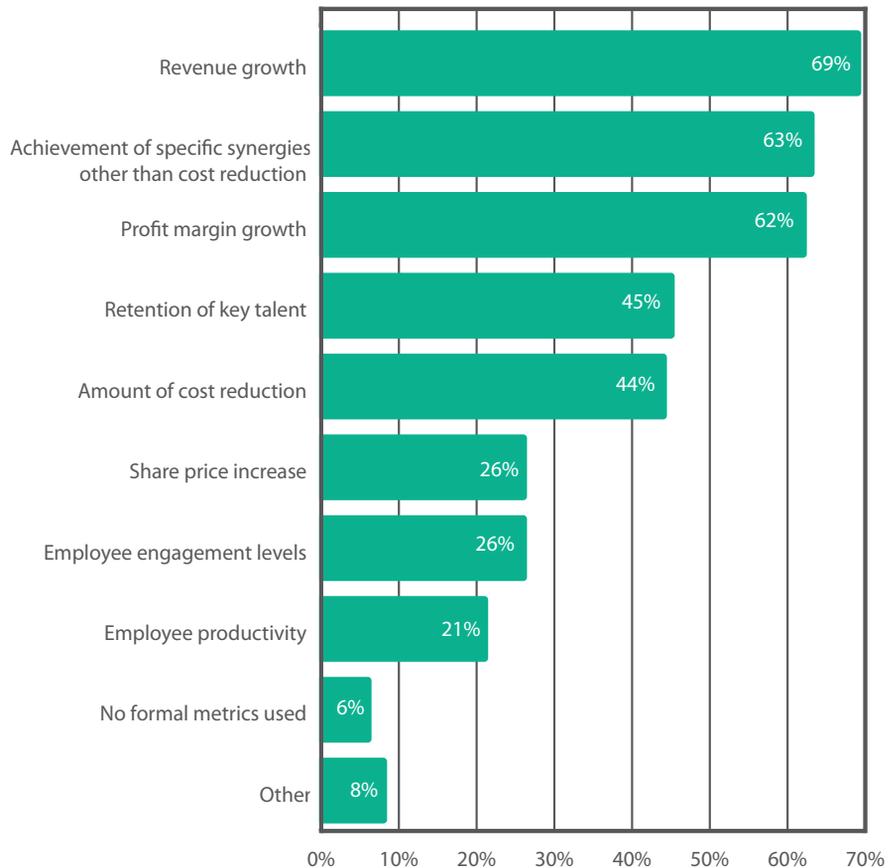


M&A PROCESSES AND GOVERNANCE

“At Quebecor World, often the acquisition was structured at a higher level, and there was no documented consideration given to human resources. There was a lot of diligence on contracts, on finance, but not enough on human capital. People in charge of integration had to resolve all the issues. Finance was responsible for identifying risk and providing valuation. Many times the human capital risk is not well identified and factored in those evaluations. If there is a risk, it should be identified by finance so it is properly taken care of in the valuation model and also in the integration plan.”

Carl Gauvreau – Principal, Gauco Inc and former CFO, Hartco Inc.

CHART 3: WHAT METRICS ARE TYPICALLY USED TO DETERMINE THE OVERALL SUCCESS OF YOUR TRANSACTIONS?



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“In our organization, once the deal is final, an integration team is put together which would include HR and operations. The key factor with respect to human capital in our organization is operations. 90% of our workforce is the front line employees. Operations takes over the integration, as well as building the relationship with human capital, in hand with HR. Our operations across the country are unionized, as a result we are likely to encounter a situation where a decision must be made based on the scope and terms of the agreement in regard to which union will represent the membership. HR has a key role, but overall, it's operations which oversees the integration.”

Hanif Ladha – VP Financial Planning & Operations Support, G4S Cash Services (Canada) Ltd.

HR was cited as being primarily responsible for assessing and mitigating the human capital risks in the context of M&A at 37% of companies. Only one in five companies said finance bore the primary responsibility. According to one forum participant, however, it's not important which department per se is in charge, as long as one senior person is overseeing the key details and managing the various moving parts. “You need someone in there that can bring all the pieces together, whether that is your integration team or whether it's the Chief Financial Officer,” notes Mark Donaghy. “It doesn't really matter, as long as somebody has recognized that there is a potential issue out there and somebody has to bring it together. It can be any of the key leaders, but somebody better take responsibility for it.”

“It's ultimately the deal guy that bears the primary responsibility. If that's the CEO, then it's usually the CEO with the help of HR, or whatever experts he's got with him on the team. It's usually finance that's running the overall process, but ultimately, I haven't seen finance as necessarily the deal person. Ultimately it's the CEO that's going to own that to make sure that the people side of it is dealt with, and it's going to fit in with the overall HR philosophies and policies.”

Laurie Tugman – Former CEO, Marsulex Inc.

“The person responsible is the CEO or the person reporting to him for the project. And generally, the measurement done afterwards was: Have we accomplished the business reason for the acquisition?”

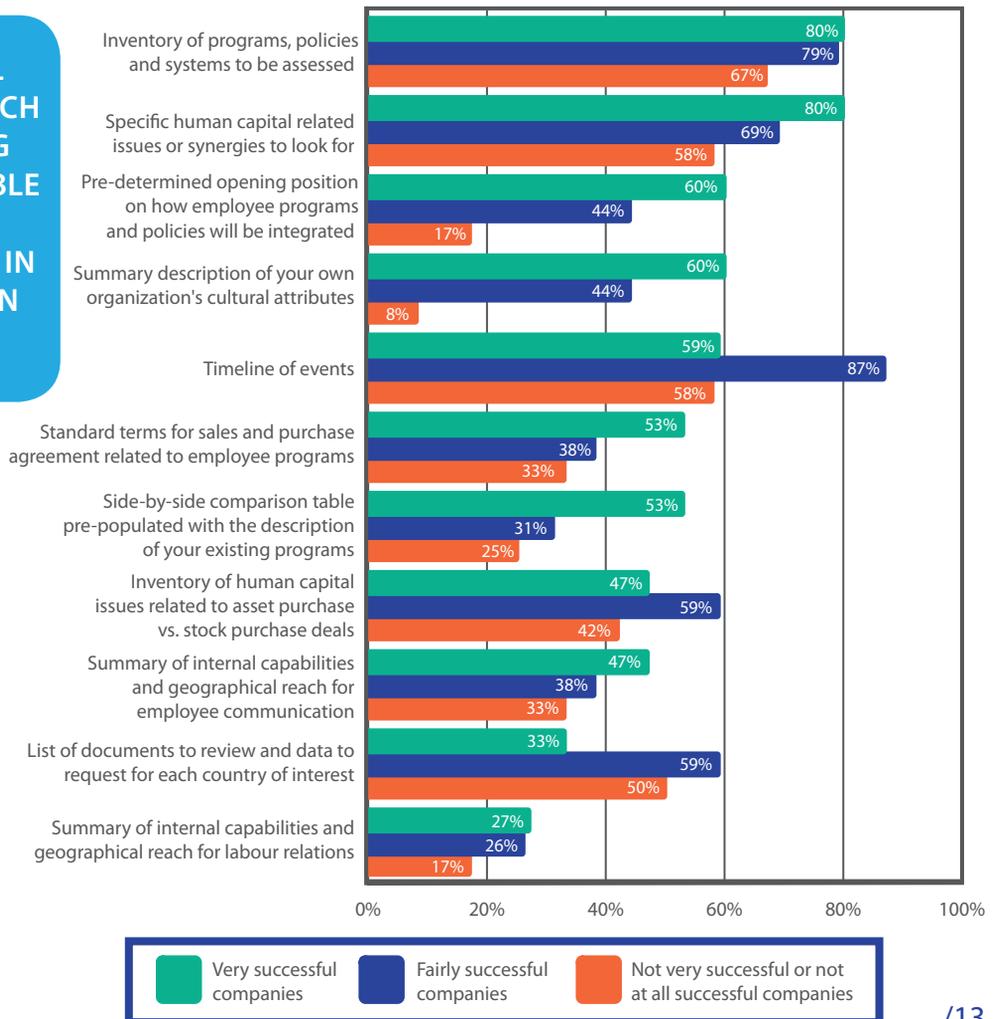
Bob Rollwagen – Consultant and retired CFO, Metro Waste Paper Recovery

DUE DILIGENCE PHASE

DUE DILIGENCE PHASE

Companies which reported that their recent M&A transactions were very successful led other companies in three areas when it came to due diligence review of human capital matters. The vast majority (87%) of the very successful companies reported having a timeline of events available prior to the due diligence review. Fewer than six in 10 companies in the less successful categories reported having timelines. See Chart 4.

CHART 4: PRE-DEAL PREPARATION: WHICH OF THE FOLLOWING ITEMS ARE AVAILABLE PRIOR TO THE DUE DILIGENCE REVIEW IN RESPECT OF HUMAN CAPITAL MATTERS?



HUMAN CAPITAL RISK IN MERGERS AND ACQUISITIONS: 2012

Eight in 10 successful companies reported having specific human capital related issues or synergies to look for, compared with seven in 10 fairly successful companies, and only six in 10 unsuccessful companies.

Finally, very successful companies reported they had already prepared – prior to the due diligence stage – an inventory of programs, policies and systems to be assessed. About the same number of fairly successful companies reported having this, but fewer (67%) unsuccessful companies.

It was interesting to note that when it came to reviewing a checklist of items during the due diligence process, 80% of the least successful companies said they looked at opportunities for cost reduction, while only 67% of the very successful companies did this. Successful companies were more likely to review individual employment contracts (80%) and legal and statutory constraints to make changes (80%).

Another important due diligence activity which was identified was the process of identifying key executives to retain, an activity cited by 87% of very successful and fairly successful companies. In comparison, only 58% of the least successful did this. Similarly, very successful and fairly successful companies identified key talent to retain (87% and 85%, respectively) while only 58% of less successful companies did this. Establishing a retention strategy was seen as important by 80% of very successful companies, while only 67% of fairly successful and least successful companies established one. Finally, eight in 10 very successful companies established a staffing needs and selection process during the due diligence review, while only 56% of fairly successful companies and 25% of the least successful companies did this.

When investigating cultural compatibility during the due diligence phase, it can be a useful idea to ask the seller to initiate an employee cultural survey. The results can be sent directly to the buyer or the representative, allowing the buyer to assess the cultural fit and the cultural risks within the organization. If the buyer is not able to get the employees on board immediately after the transaction, then it may pose what forum participant Howard Johnson, managing director of Veracap Corporate Finance Ltd., termed a “transition risk” to the organization. Such a survey benefits buyers concerned about cultural misfit as a cause of poor integration.

DUE DILIGENCE PHASE

According to Johnson, it's incumbent on the buyer to encourage the seller to facilitate cultural due diligence. "The savvy buyer is going to ask: How will you help us get comfort around cultural integration? Often times that will encourage the seller, who wants to receive a better price and better terms, to bring their key employees to meetings and make them part of the sale process," Johnson said. "Otherwise, the seller knows they're not going to get a deal done." Johnson suggested buyers may choose to mitigate employee risk by not paying full value for the target company up front, and structuring a deal so that part of it is contingent on future results. In some cases, buyers might allocate a portion of the purchase price directly to key employees as a pay to stay bonus.

“We would initially meet with the key person, and find out who the people are reporting to them. Once we've identified the individuals, we would just try to have discussions. They may not necessarily want the less senior staff to know that there's a possibility of acquisition, so it's hard getting access to those individuals.”

Oliver Hüls – Vice President and Controller, Corporate Accounting, Ameresco Canada Inc.

“The guys making the decision, the CEO, the team leader, the VP Finance, they need to understand the culture they're working with. And they need to have that down solid when they put it in their plan.”

Bob Rollwagen – Consultant and retired CFO, Metro Waste Paper Recovery

PLANNING PHASE

Organization is important to a successful integration. All very successful respondents (100%) said they had a planning template or process available to address a list of issues post closing. This compared to 87% of fairly successful companies and only 58% of the companies which reported their most recent M&A transactions were the least successful. See Chart 5.

The majority of respondents also said they had a communication strategy process or template available, geared toward the integration period (87% of both very successful and fairly successful companies). In comparison, only 42% of the least successful companies had a communication strategy process or template available before Day One.

The least successful companies also appeared to be lagging when it came to having an integration plan template – while 80% of companies with very successful M&As reported having one available before Day One, and 69% of those in the “fairly successful” category had one, only 42% of the companies with the least successful M&A transactions reported having one.

Plans to helping employees cope with change were included in the integration plans of most companies who had track records of success in M&As. It was mentioned less frequently by companies who had a history of transactions deemed fairly successful (54%) and by only 42% of companies with the least successful track records in M&As.

“Unfortunately most organizations leave integration planning as the last step in their M&A process, whereas it should be one of the first things considered. When a buyer first looks at a target company, they should ask two questions: (1) is it a strategic fit; and (2) can it be integrated effectively? If the answer to either of those questions is no, the buyer should walk away. When it comes to integration planning, the best practices I’ve seen are those companies that even before the deal closes, have developed a comprehensive 100 day plan which specifically addresses in onerous detail all of the initiatives that have to be taken. A lot of those have to do with people. Who’s going to talk to the employees; what is the communication strategy. It’s not just the employees of the target company, it’s also the buyer’s existing employees, many of whom may be sensitive or nervous. If there’s going to be some transitional pain in terms of layoffs or fundamental changes, it’s best to address those early, and treat people fairly. That will give the buyer a better chance of successful integration, as opposed to trying to cover it up and therefore suffering what usually are unintended consequences.”

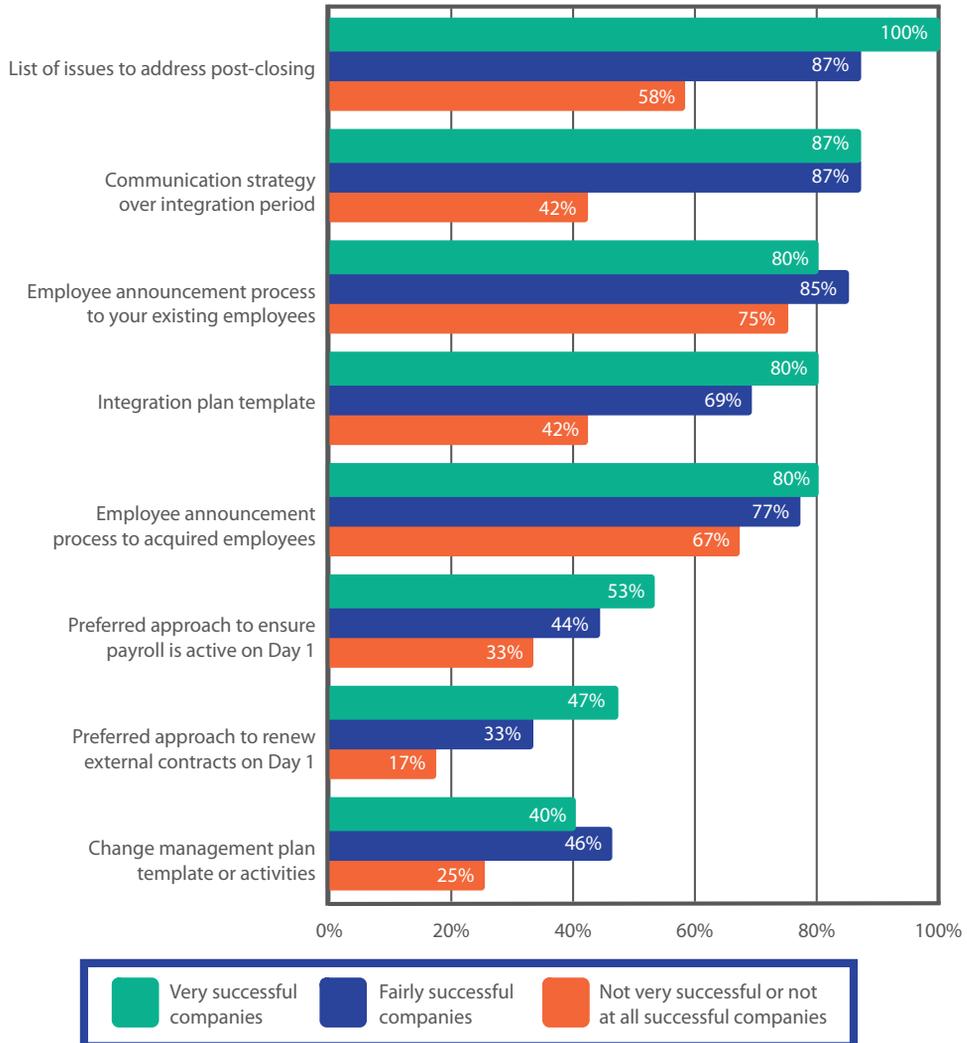
Howard Johnson – Managing Director, Veracap Corporate Finance Limited

PLANNING PHASE

“I’ve been in a very closed-off position of observation of a large public company that had a strong personality and three acquisitions failed. And they found out up to three years afterwards. It was a result of their culture just not allowing the other company’s culture to work.”

Bob Rollwagen – Consultant and retired CFO, Metro Waste Paper Recovery

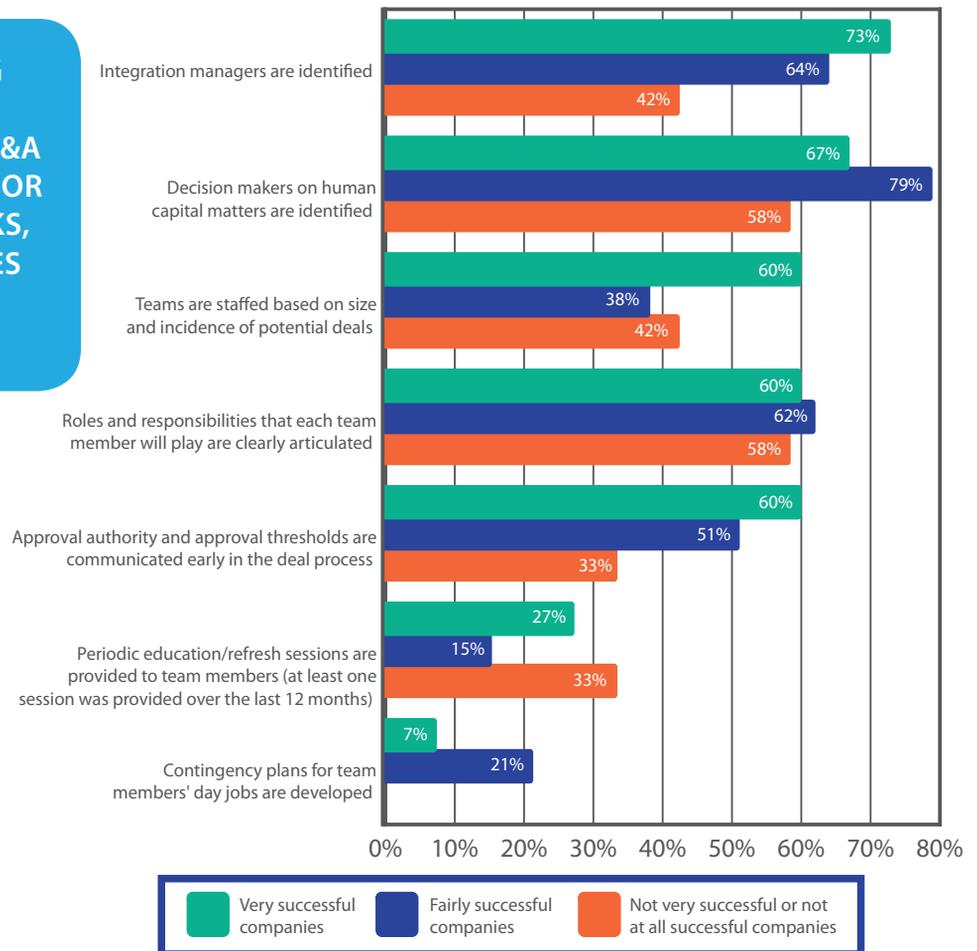
CHART 5: BEFORE DAY ONE: WHICH OF THE FOLLOWING PLANNING TEMPLATES OR PROCESSES ARE AVAILABLE BEFORE CLOSING IN RESPECT OF HUMAN CAPITAL MATTERS?



HUMAN CAPITAL RISK IN MERGERS AND ACQUISITIONS: 2012

Successful companies do several things differently when it comes to making decisions around staffing and preparing their M&A team responsible for human capital. For instance, integration managers are identified in 73% of companies with very successful transactions, but this was done by only 42% of organizations with transactions deemed not very or not at all successful. Similarly, approval authority and approval thresholds are communicated early in the deal process in six in 10 companies with very successful transactions, compared to one in three of the least successful companies. See Chart 6 for comparisons.

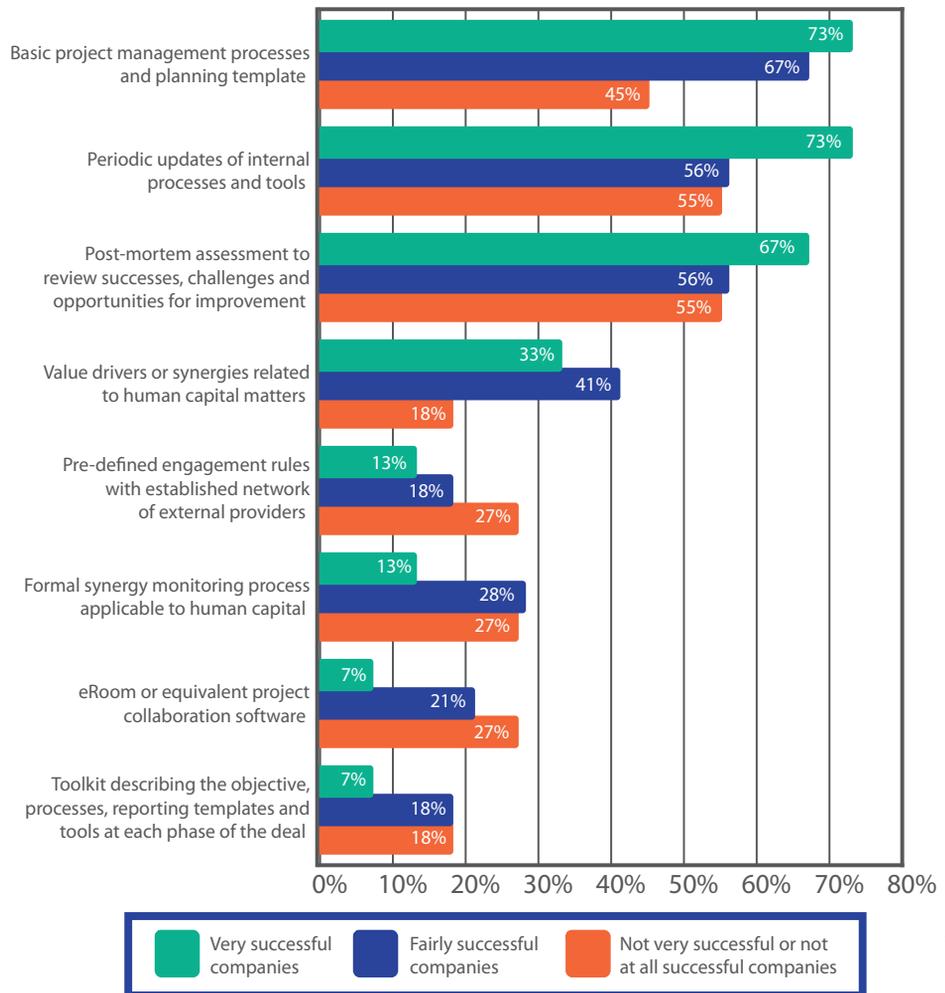
CHART 6: REGARDING GOVERNANCE AND STAFFING OF YOUR M&A TEAM RESPONSIBLE FOR HUMAN CAPITAL RISKS, SELECT ALL ACTIVITIES THAT APPLY TO YOUR ORGANIZATION:



PLANNING PHASE

In addition, 73% of very successful companies said the M&A team responsible for human capital risks used basic project management processes and planning templates in their transactions, compared to 67% for companies with fairly successful for transactions and only 45% for those that were least successful. See Chart 15.

CHART 7: WHICH OF THE FOLLOWING PROJECT MANAGEMENT PROCESSES AND TOOLS ARE AVAILABLE TO YOUR M&A TEAM RESPONSIBLE FOR HUMAN CAPITAL RISKS?



HUMAN CAPITAL RISK IN MERGERS AND ACQUISITIONS: 2012

The companies with a history of success in M&As were more likely to have a Project Management Office identify human capital risks and plan mitigation strategies. Similarly the most successful companies were more likely to ensure deliverables were on track for completion by the intended due date. The most successful companies were also more likely to have a PMO which defined and managed the scope of the project. See Chart 8.

CHART 8: PROJECT MANAGEMENT OFFICE (PMO): SELECT ALL THAT APPLY IN RESPECT OF YOUR PMO RESPONSIBLE FOR HUMAN CAPITAL MATTERS:

Project Management Office (PMO): Select all that apply in respect of your PMO responsible for human capital matters:	Very successful*	Fairly successful*	Not very or not at all successful*
Identify risks and plan mitigation	80%	76%	60%
Ensure the deliverables are on track for completion by intended due date	80%	67%	60%
Have representation at critical decision-making sessions	70%	70%	70%
Define and manage the project scope	70%	61%	50%
Perform other activities not listed above	10%	30%	30%

Integration

“You’ve got to communicate and measure productivity. You want employee programs harmonized in the first few months. As far as employees are concerned, it should be known Day One what you’re going to do, and you’re going to do it as quickly as possible. Culture takes a lot longer than anybody ever thinks.”

Laurie Tugman – Former CEO, Marsulex Inc.

IMPLEMENTATION PHASE

IMPLEMENTATION PHASE

Companies with a history of greatest success in M&As were more likely to review or harmonize benefits programs in the first two years after closing. 93% of companies which were “very successful” in past transactions did this, compared to only 58% of companies with the least success in past transactions.

Two merger stories

“Our company merged with another company. Our company was doing extremely well in the market and had very generous benefits programs and being the leader within the merger we opted to provide them with the same benefits that we had which were as good as theirs. After a thorough due diligence of the business and their compensation/benefits plan, we concluded we could migrate them to our plans at a better price. We had all our group benefits at 100% coverage on general dental and health programs and large lifetime coverage for items like crowns and braces. They also had a RRSP employer sponsored plan. Again we had the better plan. We merged the two. We froze salaries until certain employees lined up with other employees. We continued to offer generous benefits and we did not have a lot of downsizing and as the business was slowly being restructured, the merged employees looked at it as an opportunity to refine their skills. As most of this merger was led by finance, which was also responsible for HR, benefits and administration, I can say the merging of the two cultures was done smoothly.”

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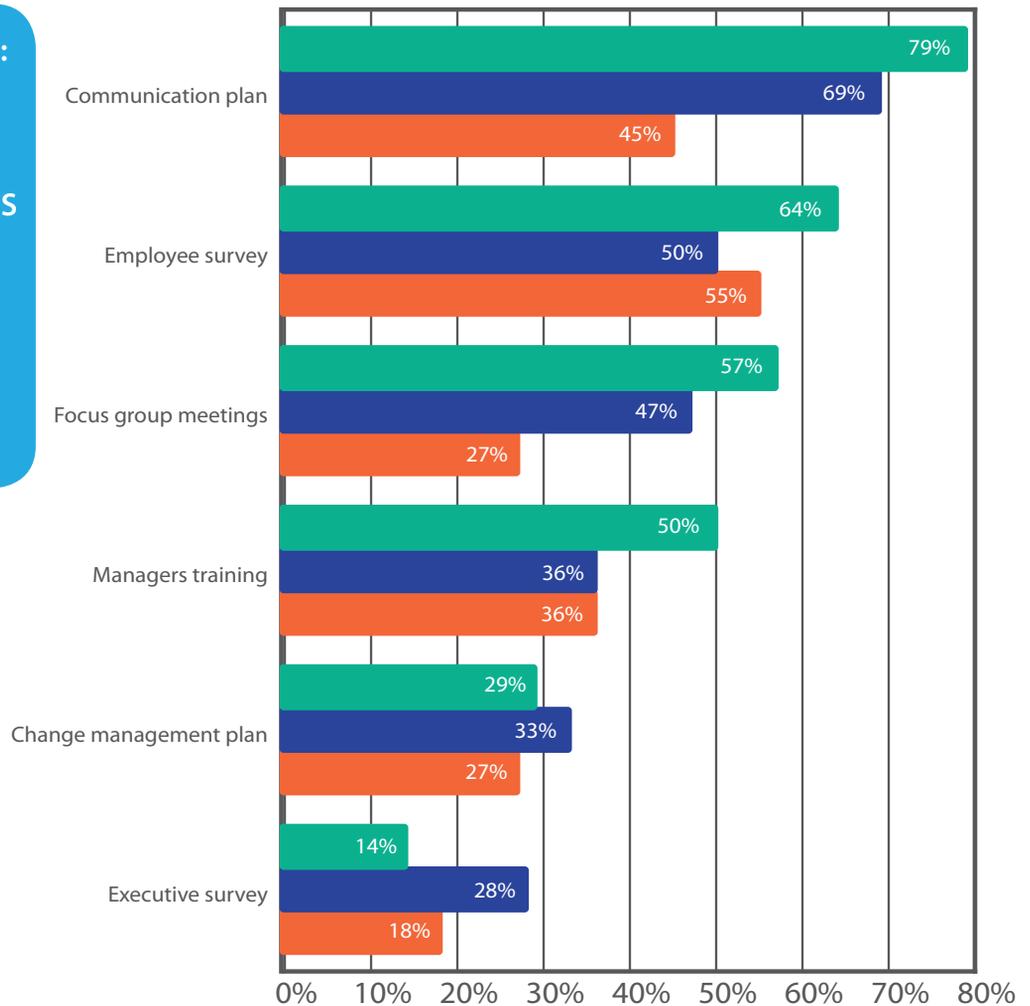
“In a merger of three companies, the smaller companies were charged for shared-services – larger fees than they used to pay for payroll processing, benefits administration, retirement plan administration, IT services. They paid substantially more for less leading to very disgruntled employees. The mandate was to do the reorganization at all costs but people were not considered. On a long-term basis this approach has significantly affected the success of the North American companies as it is said that the success of companies is mostly attributable to how engaged and happy employees are.”

Interviews with senior financial executives

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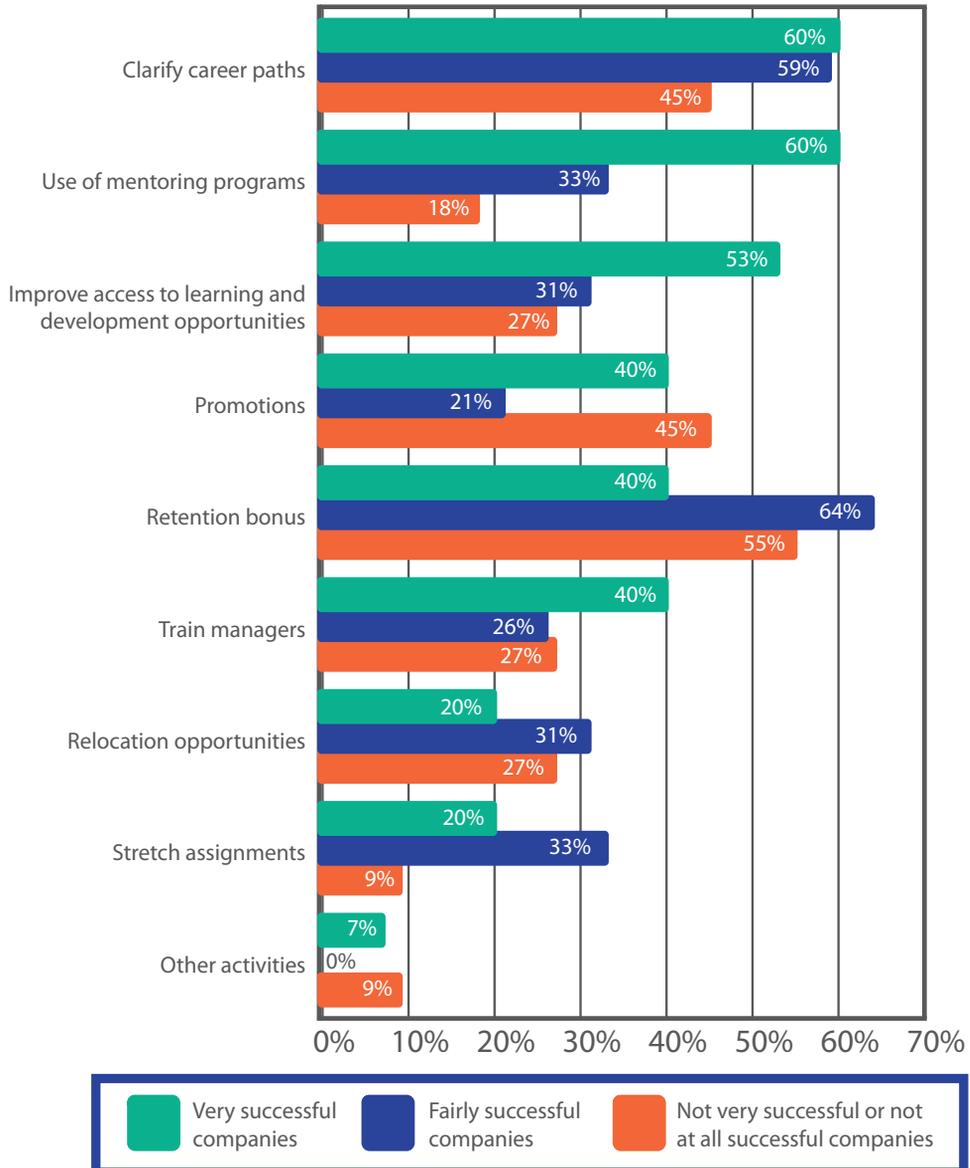
Using a communication plan and employee survey to assess cultural differences were strategies more likely to be used by companies with the most success in M&As. For instance, 79% of very successful companies used a communication plan, and 64% used an employee survey, compared to only 45% and 55% respectively, of the least successful companies. See Chart 9.

**CHART 9: CULTURE:
WHICH OF THE
FOLLOWING
APPROACHES DO
YOU USE TO ASSESS
AND ADDRESS
CULTURAL
DIFFERENCES
DURING THE
INTEGRATION
PERIOD?**



IMPLEMENTATION PHASE

CHART 10: TALENT RETENTION: WHAT ACTIONS ARE USUALLY IMPLEMENTED TO ADDRESS KEY TALENT OR EXECUTIVE RETENTION DURING THE INTEGRATION PERIOD?



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Talent retention strategies such as clarifying career paths, mentoring programs and improving access to learning and development opportunities were more likely to be used by companies with the highest success rates in previous M&As. (See Chart 10) For instance, 60% of very successful companies used mentoring programs, while only 18% of the least successful companies did so. Vicki Nishimura, of Prism Medical, has used incentives such as retention and stay bonuses to keep key employees during past transactions. "It is essential to keep the business operating and to do so, we have learned that unless you have the engagement and more importantly, the trust of employees, then no matter what you do, you're not going to have a successful integration. Effective communication helps promotes this trust. It's listening to their concerns, responding and monitoring them, which will gain their trust," she said, adding a combination of various measurement and performance tools were used to track employee engagement and productivity.

According to Derek Petridis, of Shikatani Lacroix Brandesign, the key incentive for most employees is financial, so the company offered profit sharing to new employees post-acquisition. "All this other stuff is great, but at the end of the day, people go to work for money," he said.

During the integration period, frequent communication from leadership was a tactic commonly used by

companies with a very successful track record in M&A (93% of very successful companies, compared to 74% of fairly successful ones, and only 58% of not very successful companies). See Chart 11. One forum participant wondered how to communicate when staff retention decisions have not yet been made. "How do you keep the communication transparent when post acquisition you do have some secrecy about who to keep, who to let go, and how to avoid creating a difficult atmosphere for the first 100 days. Most of the time I think people are left to survive on their own and they don't understand what's going on. They are trying to survive and a lot were just leaving before the buyers

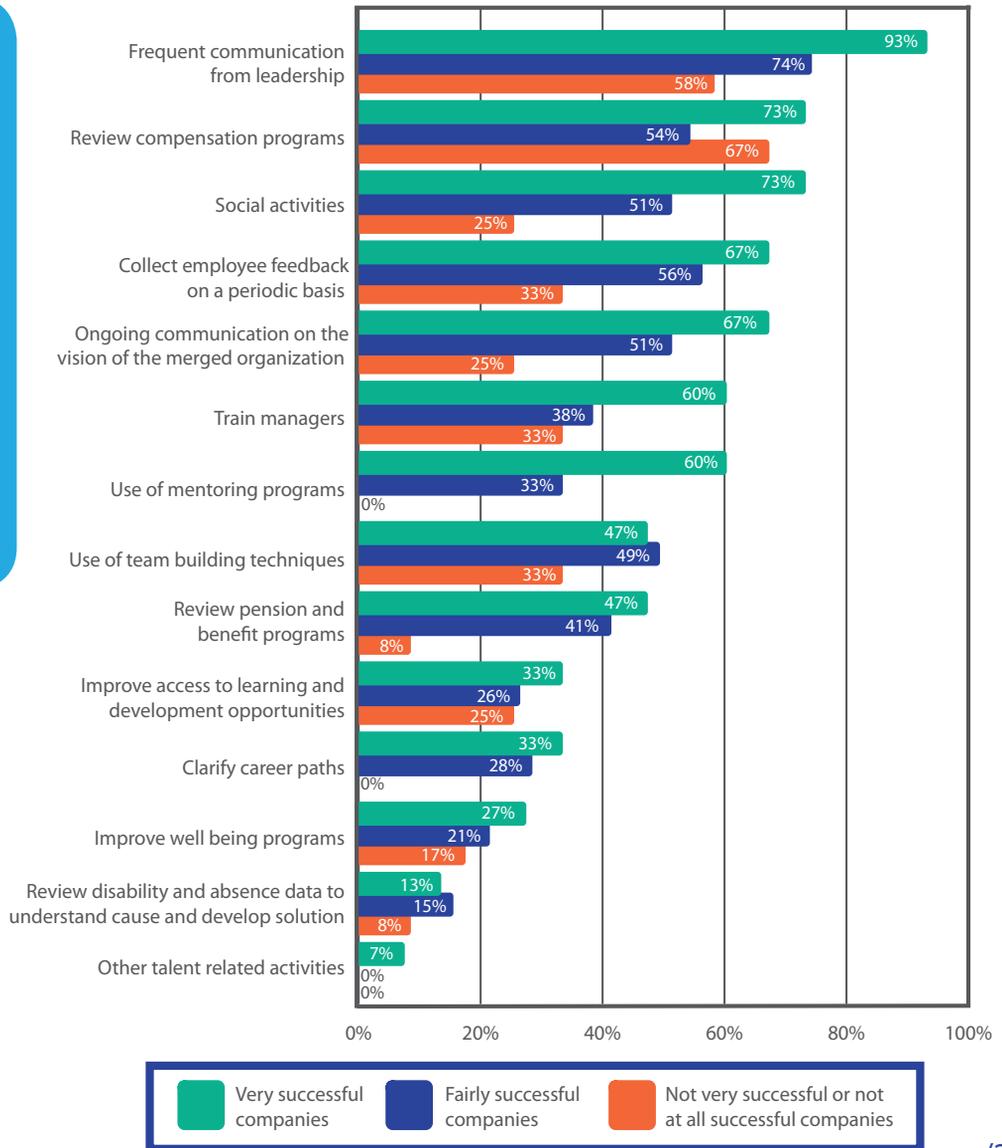
“Put yourself in the seat of the employees and ask yourself the question: ‘What’s in it for them?’ Whether it’s cash or something else, that’s really the core question.”

Peter Lane – Former SVP Finance and Administration at Canadian Tire Corporation Retail Division

IMPLEMENTATION PHASE

or people of the other company even picked out who are the key people.” Other forum participants agreed it was best to communicate with staff up front as quickly as possible.

**CHART 11:
EMPLOYEE
PRODUCTIVITY:
WHAT ACTIONS
ARE USUALLY
IMPLEMENTED
TO IMPROVE
EMPLOYEE
ENGAGEMENT
AND
PRODUCTIVITY
DURING THE
INTEGRATION
PERIOD?**



Communication

“Accountabilities amongst all the people that are going to be going in to work on the integration of the company should be clearly defined. Unintentional misinformation can be very damaging. If you’re in there and you’re working on something on IT and somebody’s asking you about something that’s HR related, don’t assume. Don’t guess. Say here’s the person to talk to in HR, and perhaps have an employee hotline.”

Cliff Truax – Director, Financial Services & Regulatory Affairs, Hydro One Telecom Inc.

Talent retention

“Talent retention is no different than before acquisition. If you had low turnover because you’ve got good HR programs and policies, and you do all of these things, you’ll have low turnover post-acquisition, because you should have a good reputation. What’s your organization’s brand when it comes to people? Are you known as a place where people want to work? That’s going to be known Day One, and you’re not going to change that with an acquisition.”

Laurie Tugman – Former CEO, Marsulex

Talent retention

“There are two types of buyers – the direct competitor, which often employs a slash and burn approach, and assesses risk from the perspective of employee lawsuits. And then you have the platform buyer, which is interested in generating incremental revenue by leveraging the target company’s product and service offerings, employees and customers. The risk to the platform buyer is erosion of intangible value, or goodwill. Intangibles such as brand names or proprietary technology tend to remain intact. The greater risk relates to employees and customers, which are inextricably intertwined. In a privately-held business, goodwill often resides in the owner. If they receive a large payment at closing, they might leave soon after or become disengaged. In some cases there are a handful of key employees who have strong customer connections or technical knowledge. The buyer needs to identify key people, relationships, and knowledge that would be difficult to replace, particularly if they left for a competitor.”

Howard Johnson – Managing Director, Veracap Corporate Finance Limited

Culture

“We did an acquisition in Quebec. There were cultural and language barriers. So you try to have open communication until the employees from Quebec phone the HR director, who happens to be located in Toronto. Well, they speak French and this person speaks English. So they’re both frustrated. Employees aren’t getting the answer and the director is frustrated because he or she, even though willing, can’t communicate effectively.”

Oliver Hüls – Vice President and Controller, Corporate Accounting, Ameresco Canada Inc.

CONCLUSION

CONCLUSION

Human capital risk stands out as an area that requires attention when an organization enters a period of transition. Even as a company contemplates involvement in an M&A, any preliminary activity will have a ripple effect on employees. This brings with it risks and responsibilities to manage those risks.

Along with ensuring a potential acquisition is a strategic fit, companies must assess whether the company is a candidate for successful integration in areas such as corporate culture, being able to retain key talent and harmonization of employee programs.

Companies must be aware of a myriad of potential human capital risks before even entering a due diligence process. Before their next transaction, organizations should assess how ready they are to identify and address human capital risks.

When staffing and preparing their M&A team which will be responsible for human capital, companies should identify an integration manager, and equip the team with project management processes and planning templates.

When undertaking due diligence, organizations would benefit from using a pre-prepared of list programs, policies and systems to be assessed, an estimated timeline of events, and they should seek specific synergies in human resources. Due diligence is also the time to establish and prioritize a retention strategy, which should include steps to identify and retain key executives and other key talent. The retention strategy forms part of a greater overview of staffing that need to be addressed during due diligence.

Organization and planning tools continue to be critical when planning for integration. Again, a template or process should be used to prepare and prioritize issues to be addressed after the deal is closed. An integration plan – including plans to help employees cope with change – and a communications strategy to convey the plans should also be ready before Day One.

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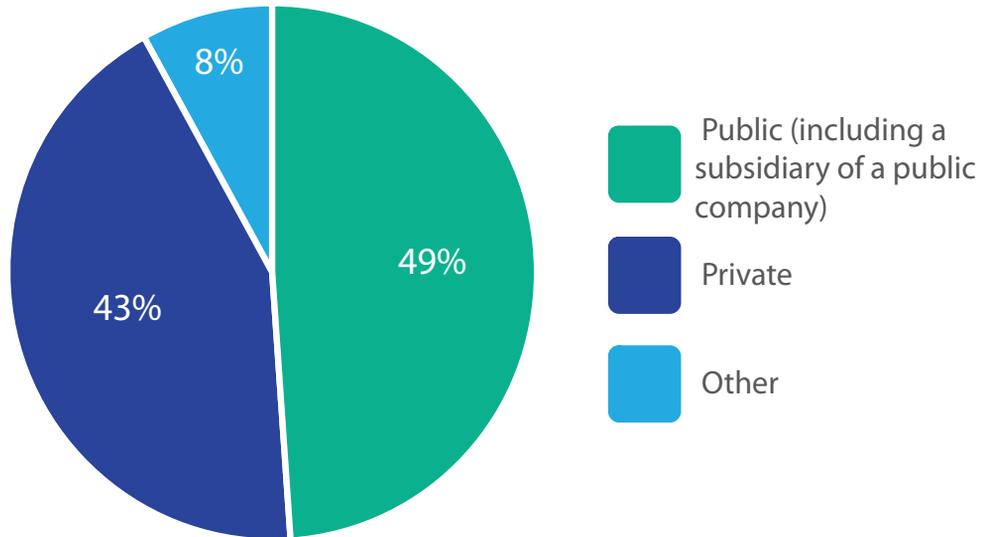
Based on the strategies outlined above, it appears that the companies which were most diligent about planning, using tools such as timelines and planning templates, well before the integration stage, will be best positioned for a successful M&A. It's therefore clear that an early assessment of the likelihood of integration success must be undertaken at the due diligence stage, not after Day One.

During implementation, companies should review and harmonize benefits programs within two years after closing. Communication by leadership should be a priority. When managing cultural integration, tools such as a communication plan, employee surveys, focus group meetings and manager training can be employed. Some methods of supporting talent retention during implementation include clarifying career paths, mentoring programs and improving access to learning and development opportunities.

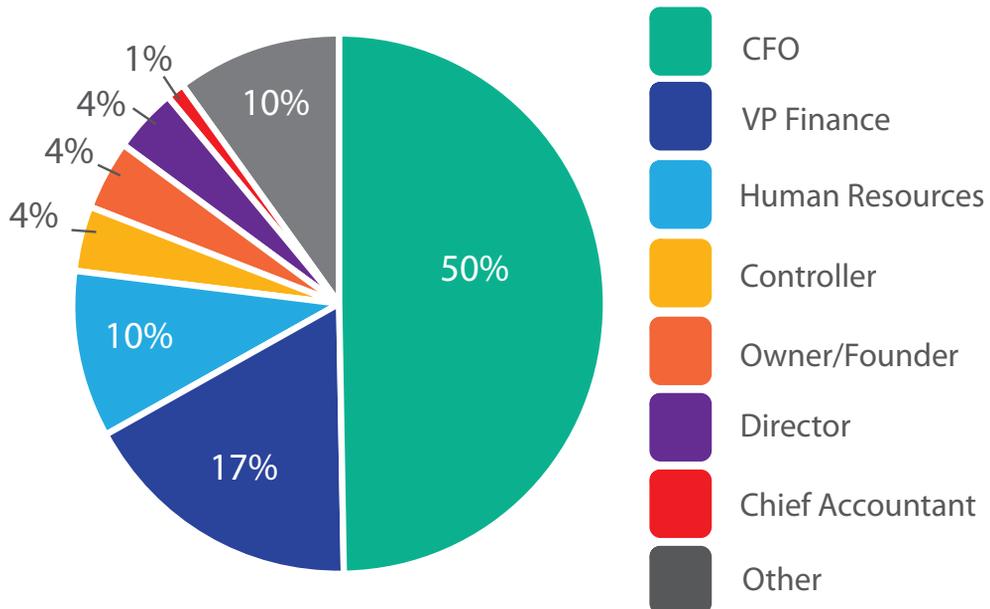
APPENDIX A: SURVEY DEMOGRAPHICS

APPENDIX A: SURVEY DEMOGRAPHICS

CORPORATE STRUCTURE

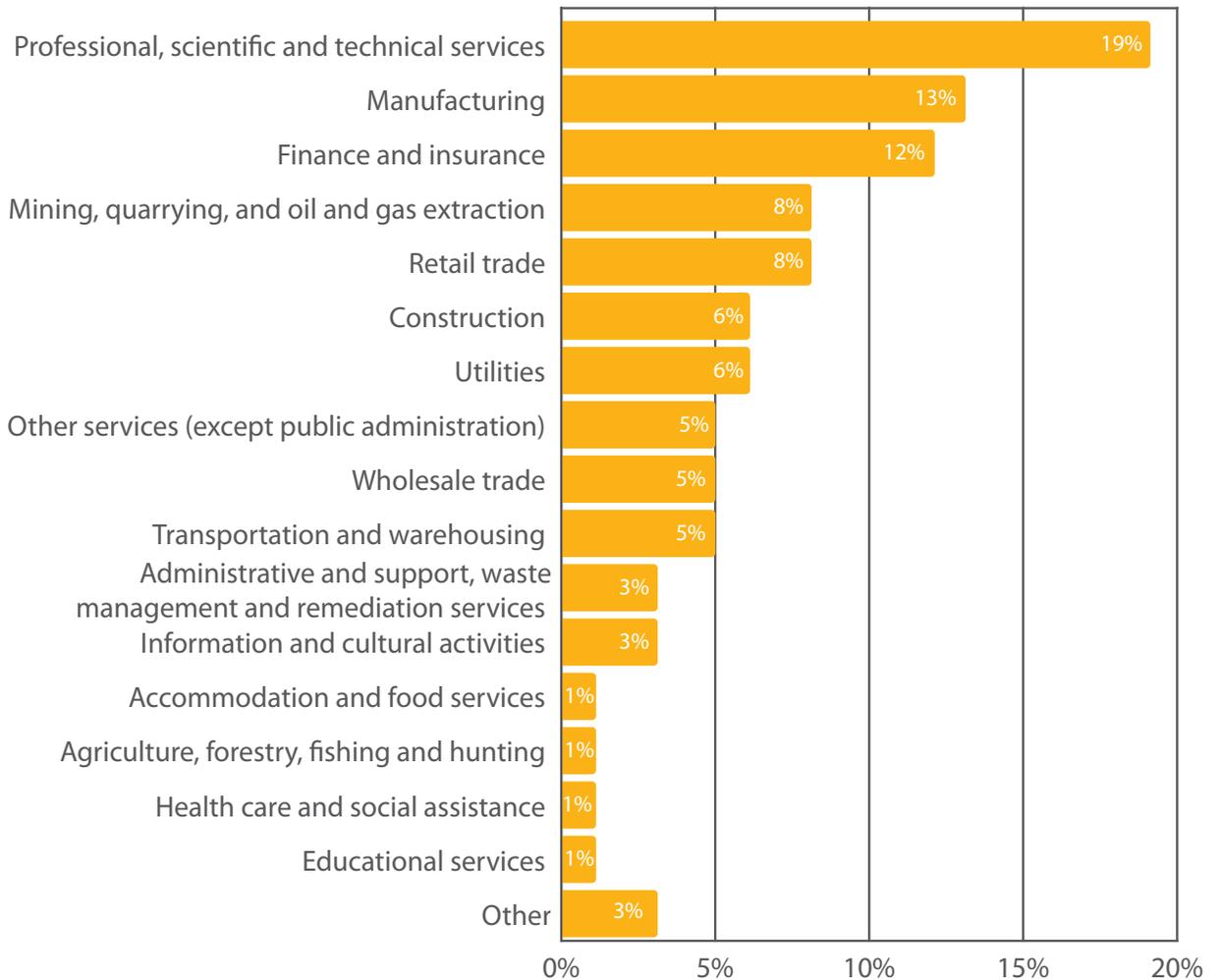


POSITION TITLE



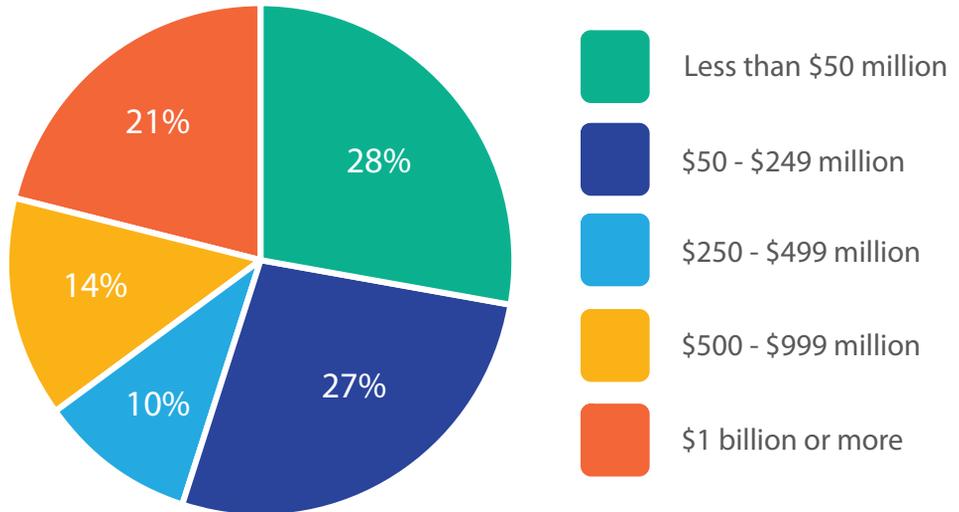
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INDUSTRY CLASSIFICATION

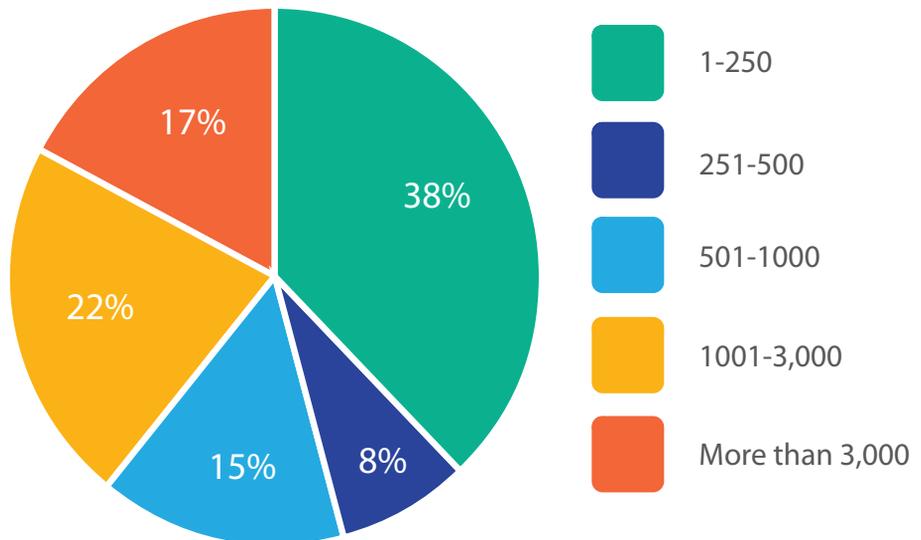


APPENDIX A: SURVEY DEMOGRAPHICS

ANNUAL REVENUE



EMPLOYEES



APPENDIX B: FORUM PARTICIPANTS

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Moderators:

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Oliver Hüls – Vice President and Controller, Corporate Accounting, Ameresco Canada Inc.

Howard Johnson – Managing Director, Veracap Corporate Finance Limited

Hanif Ladha – VP Financial Planning & Operations Support, G4S Cash Services (Canada) Ltd.

Peter Lane – Director & Treasurer, Mood Disorders Association of Ontario

Amit Loomba – Director & Team Leader, Commercial Banking, CIBC

Vicki Nishimura – VP Corporate Controller, Prism Medical Ltd.

Derek Petridis – VP Finance, Shikatani Lacroix Brandesign

Bob Rollwagen – Consultant and retired CFO, Metro Waste Paper Recovery

Cliff Truax – Director, Financial Services & Regulatory Affairs, Hydro One Telecom Inc.

Laurie Tugman – Former Chief Executive Officer, Marsulex Inc.

APPENDIX B: FORUM PARTICIPANTS

By telephone:

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