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Article 3: Governing the Transition stage

This is the third article in a quintet of articles on board governance of M&A, published by the AICD Governance Leadership Centre.

By way of a brief recap, the full M&A lifecycle can be divided into the following four stages:

1. Targeting (including development of the M&A intent and strategy)
2. Transaction (the deal)
3. Transition (post-deal, or the first 100–180 days)
4. Transformation of the combined enterprise.

Article 1 of the series commenced with an encouragement for executives and boards to begin with the end in mind. Consistent with that approach, Article 2 commenced at the final stage of the M&A lifecycle, **Transformation,** and encouraged executives and boards to think deeply about the purpose of the acquisition and what the intended outcomes of the transaction were. During the Transformation stage, it is important that executives and boards maintain drive and focus to ensure that the intended outcomes of the acquisition are delivered.

This third article relates to the third stage of the M&A lifecycle, **Transition**. The Transition stage commences with go-live or Day 1 of the new entity's ownership and continues for circa 180 days to bed down the initial wave or waves of changes for the acquisition.

First, some words from the wise

"The nicest thing about not planning is that failure comes as a complete surprise and is not preceded by a period of worry and depression."

[John Preston, Boston College]

It is important in the Transition stage that:
- the executive team mobilises sufficiently early, in a structured and deliberate way, to secure the sources of value originally targeted at the time of commercial due diligence; and
- integration proceeds in a manner that causes as little disruption as possible to customers and operations (so there are limited dis-synergies).

The board's role is to challenge and coach the executive team as it ensures Day 1-100 readiness and undertakes post-merger integration activities.

Why is this stage so important?

The first reason is that time is money. Whatever the quantum of the purchase price, losing 3-6 months due to dithering, false starts or wrong turns means the acquirer is even further behind in recouping the control premium paid as part of its capital outlay. It can be incredibly hard to recover the time and momentum lost after deal closure.

Ideally, Transition preparation would commence during the transaction (Stage 2). It would involve planning activities, setting up of the transition programme governance, planned resourcing, and development of a target operating model. Commencing these activities early means you not only have a jump start on Stage 3, but they may also help inform consideration of the bid price.

Secondly and directly related, is confidence. The management team needs to allay fears among staff, shareholders, customers etc. and show that it is in control, working to a plan, and mobilised instead of dithering.

The third reason why this stage is crucial is the discovery that now occurs about the condition of the acquired business. This is the stage where the pre-deal unknowns start to become clearer, and further unknowns may emerge. There are always going to be surprises, particularly if this has been a hostile acquisition or one involving limited due diligence.

What does the board need to do?

The board should be well aware that the executive team is in the 'honeymoon period' post deal, but that the clock is ticking.

There are a number of activities by the executive team that are imperative during this stage: the execution of and ongoing refinements to a cohesive plan with clear accountabilities; active monitoring and checking of working assumptions and unknowns; and having a target operating model blueprint to help navigate the transition.

The board needs to enquire about, review and monitor the progress of these activities. How realistic are these plans? Where are the likely pinch points? What are the early signs of danger?

In my view, part of what an effective board does is to work with the CEO to 'move the worry curve to the left'; that is, so that the executive feels the heat of collective board and investor expectations.

The board should also agree with management a set of guiding principles, philosophies about integration, and parameters for the deal transition.

> As one highly experienced director put it:
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> *"And they came back with what we called our principles diagram. And …the number of times ….when the going got tough in the integration, we kept putting the principles on the table and saying, what we agree is a principle was this… So most people then say we'll have best of breed, which I think is a grossly overused phrase. We adopted a principle that it's A or B not C. If you then compromise and don't make the hard decisions, you create the best of breed which is now a pale blue one, and your cost synergies go out the door...."*

Effective boards are aligned with the CEO on what I call the 'value scorecard', and insist on regular updates on how delivery of the targeted benefits is tracking. The baseline for benefits realisation, the plans, project management, and governance mechanisms to manage value delivery, must all be put in place during this stage (if not already done so).

Another experienced director noted:

"…having made the investment, the board should set up as part of its process and due governance an asset and investment review at regular intervals and of course people are a lot more enthusiastic about buying things than they are about reviewing their purchases."

What typically goes wrong?

There are typically three areas where problems arise.

Firstly, lack of intentionality - operating with hope more than intent. This might include lack of a clear plan, loose or no accountability, deficiencies in adequately skilled and available resources, or having no organisational and operating blueprint to work to. This doesn't mean that the executive should force, or be fixated on, post-merger integration. Particularly when acquiring new capabilities or skills, trying to engineer alignment can be entirely counter-productive. So it does require forethought, planning, design and deliberateness in acting (or not acting).

Second, complacency, or, conversely, over-haste. The former might manifest as slow and disjointed mobilisation, and the latter as rapid action without enough forethought and communication.

Third, inept stakeholder management. This might include an absence of clear messaging and 'reach-out' activities to staff 'captured' in the acquisition, as well as the acquirer's staff, causing doubt, uncertainty and fear.

As a result of any or all of these occurrences, any 'grace period' given by the market place could be squandered.

So what are the key things boards should be looking out for in this stage?

1. Management is working to a plan – there is deliberateness and a level of coordination appropriate to the kinds of post-merger activities needed to stabilise and align the acquired entity with the acquirer (note: integration is not always an appropriate activity – it all depends).
2. Governance is in place for the Transition programme – clear accountabilities, milestones, checks and

Transition Stage

Tips and Traps

What to do right: conditions for success

1. Executive must be in ownership
2. Understand the complexity
3. Select fit for purpose project controls
4. Communicate, communicate, communicate - manage the journey

What to look out for:

5. Under-estimating the importance of culture and journey management
6. A conspiracy of optimism – "this will be easy"
7. Part-time resources and lack of accountability

Remember:

8. Limited overs cricket – run rate really matters
9. Keep coming back to the outcome - laser like focus on outcomes
10. Deal making was the easy part
11. The soft factors are the hard factors

balances, and resourcing as needed.

3. Front of mind consciousness of the time value of money – management understands that the clock is ticking, investors are watching, and that it is important to lay a foundation for future value. This doesn't mean that management should be 'going like a bull at the gate' – sometimes you need to go slow to go fast.
4. Suitable resources – skills, depth of experience and numbers – are being committed to securing or enhancing the value targeted in the baseline business case.

Those organisations that approach this stage with a project delivery mindset have a distinct advantage. The board should encourage management to do a readiness review of the portfolio of post-merger initiatives to understand their overall complexity and the extent to which the portfolio is being set up for success.

Such an understanding of portfolio complexity will help determine what level of capabilities and project controls are needed for the challenges ahead; capabilities such as leadership, governance and oversight, risk management, resource management, delivery management and reporting, business unit involvements etc. The board should have confidence that capabilities and project controls are suited to the task ahead.

> As one director put it:
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> *"So I think one of the great skills that is needed in the whole M&A agenda is project management..... I passionately believe it..... So I've put my bias on the table. But if you just think about the …merger with [Co. Y]…., one of the senior team ….was the full time integration manager. We had 54 different projects, separate projects underway and this is in the next phase of the integration of, once you've done the deal and somebody's signed the cheque, then …that's only just the start."*

If there is one thing a board needs to do well at this stage, it is to ensure that management is going into this 'eyes wide open and prepared' and has a laser-like focus on targeted benefits.

Test yourself with five key moment of truth questions

To conclude the Transition stage, ask yourself five critical questions on how you and your fellow board members govern 'post transaction value delivery':

1.	Does the executive team have clear targets for value delivery and does the board understand the basis and working assumptions behind these?	✓
2.	Is the sponsor and executive team committed to deliver the agreed-upon outcomes and do they have clear accountabilities and decision-making rights in place?	✓
3.	Does the executive team have a portfolio of initiatives, plans and resources lined up to support and deliver the value targets?	✓
4.	Can we confidently commit on these plans to our shareholders? Would our plans convince a sceptical market?	✓
5.	Have we really thought through what could go wrong and are we, as the board and executive team, clear on our critical assumptions and unknowns?	✓

Think about these five questions. We will invite you to take a short survey at the end of the final article to assess how M&A capable and prepared your board is.