2003

Human resources' role in successful mergers and acquisitions

Vanessa Loecke

University of Northern Iowa

Follow this and additional works at: https://scholarworks.uni.edu/pst

Let us know how access to this document benefits you

Recommended Citation

https://scholarworks.uni.edu/pst/103

This Open Access Presidential Scholars Thesis is brought to you for free and open access by the University Honors Program at UNI ScholarWorks. It has been accepted for inclusion in Presidential Scholars Theses (1990 – 2006) by an authorized administrator of UNI ScholarWorks. For more information, please contact scholarworks@uni.edu.
Vanessa Loecke

Human Resources’ Role in

Successful Mergers and Acquisitions

April 25, 2003
Introduction

In today’s world of big business, which evolves around new technology, difficult competition, and the desire to be the biggest and the best, it’s easy to see how companies get carried away by their desire to grow vastly and rapidly. Often times, these objectives are most easily accomplished by merging with, or acquiring other companies. However, many companies also fail to merge or acquire successfully. In fact, according to a study done by BusinessWeek, 61% of acquisitions destroyed shareholder wealth (Henry, 2002).

It is for this reason that mergers and acquisitions must by analyzed more carefully, including why they fail and what can be done to make them more successful. More specifically, the integration process, which closely involves the Human Resources Department and considers the importance of corporate culture and communication, is essential in bringing about successful mergers and acquisitions.

In analyzing mergers and acquisitions, two research questions much be addressed. First, “Why do mergers and acquisitions fail?” And second, “What can be done to help mergers and acquisitions succeed?” In reviewing the second question, discovering what the Human Resources Department can do to aid in successful mergers and acquisitions is extremely important, based on a Forbes survey that found that “people-related” issues are the top reason mergers and acquisitions fail (Price & Walker, 2000).

In order to determine why mergers and acquisitions fail, mergers and acquisitions must first be defined. Then, the reasons companies merge, as well as other factors resulting in mergers, must be explored. Next, reasons why mergers fail, including financial, cultural, and evaluative reasons, are identified. These three major reasons are also explored in terms of how they can help mergers and acquisitions succeed.
More specifically, what the Human Resources Department can do to aid in a successful merger is identified, including getting involved early, conducting due diligence, aiding in integration, and communicating to employees. Finally, to bring theories to life, two case studies, the AOL Time Warner merger, and the Hewlett-Packard Compaq merger, are evaluated in terms of what the companies did wrong or right during the merger to get them in the positions they are today.

The results overwhelming support that the Human Resources Department must be deeply involved in the merger or acquisitions process for mergers and acquisitions to be successful. Furthermore, every aspect of the companies involved must be fully evaluated to determine if the merger or acquisition is a good idea. Companies must also not be influenced by outside factors when deciding whether to merge. With a great deal of evaluating and planning, mergers and acquisitions would have a greater probability of succeeding.

**Definitions of Mergers and Acquisitions**

Because both mergers and acquisitions are plagued by the same problems, the factors that contribute to their success are also the same. Thus mergers and acquisitions will be used interchangeably throughout this paper. However, there are differences between mergers and acquisitions that should be clarified for basic knowledge purposes.

A merger is when two separate companies join to form a new, third company by combining the companies. Although many mergers claim to be a “merger of equals,” with both companies having an equal stake in the new company, a true merger of equals rarely occurs. In mergers, one company usually acquires the stock of another. For
example, in a forward merger the target company receives the acquirer’s stock. In a reverse merger, the acquirer receives the target’s stock. Therefore, a selling point of merging, verses acquiring, is that it doesn’t require cash. However, mergers often become pricey due to the due diligence and legal expenses accumulated by both companies during the merger (Mastracchio & Zunitch, 2002).

Acquisitions, on the other hand, involve one company assimilating another company. Acquisitions occur through either stock acquisitions or asset purchases. In a stock acquisition, the acquiring company buys all of the target company’s common stock. Thus, the acquiring company obtains the entire target company, whether it wants all of it or not. In an asset purchase the acquiring company and the target company negotiate which parts of the company will be acquired and for how much. In this arrangement, the acquiring company has the opportunity only to take the parts of the company it wants (Mastracchio & Zunitch, 2002).

Mergers and acquisitions have become a big fad in the business world during the past eight years. In fact, from 1998 to 2000, the busiest three years for mergers and acquisitions, almost $4 trillion dollars changed hands because of mergers and acquisitions (Henry, 2002). However, as mentioned earlier, mergers and acquisitions fail. In addition to approximately 61% of mergers and acquisitions failing to increase shareholder value, the returns these stockholders receive is about 25% less than that of stockholders investing in other companies in the same industry (Henry, 2002). Further, a study conducted by Dr. Patricia Whalen found that one-third of all mergers and acquisitions are re-sold in down scoping attempts within the first five years of the merger (Mergers, 2002).
Reasons Companies Merge

If mergers and acquisitions have historically been such disasters, why are companies still considering them a viable plan? In general, mergers and acquisitions have the potential to add much value to a firm if the merger is analyzed, planned for, and implemented correctly. Companies may want to merge for a plethora of value-adding reasons. However, most of these reasons can be categorized into either striving to gain efficiency or trying to improve leverage.

Efficiency occurs when the merging companies are able to cut costs by integrating the resources of both companies, and are therefore able to condense people, processes, equipment, and other resources that overlap. Efficiencies are usually found by reducing headcount, facilities, and technology, and by integrating supplier relations and distribution (Smallwood & Ulrich, 2002).

It’s easy to see that when companies merge there would be an initial duplication of jobs. For example, a company doesn’t need, nor can sustain, two CEOs. For this reason, after mergers or acquisitions many companies downsize in an attempt to increase efficiency by running the combined company with less manpower than the previous two companies. Stemming from the reduction of manpower, the newly-integrated company may also be able to reduce the amount of facilities needed, since it no longer needs to house so many employees.

Another area merged companies hope to obtain efficiency in is technology. For example, companies may plan to consolidate their technology into a few software programs. Although this is easier said then done, it’s necessary for the merged
company’s software to be consistent, or at least compatible. Although only buying a couple software programs creates efficiency in itself, efficiency is further realized by the combined companies needing less technical support, resulting in the reduction of headcount in the information technology department.

The fourth area of gained efficiency is in supplier relations. The bigger company may be able to consolidate its suppliers, thus ordering in higher quantities from fewer suppliers. This can lead to cost savings in a couple ways. First, discounts often apply when buying in bulk. Second, there will be fewer shipping charges if the combined companies can get their supplies from fewer suppliers, and get all supplies shipped at once. Similarly, the merged company is able to gain efficiencies through its distribution system. Again, shipping charges will be cheaper if the companies can consolidate their routes and channels (Smallwood & Ulrich, 2002).

Leverage occurs when combining two companies makes the combined company more valuable than the two separate companies due to the sharing of resources, such as ideas, products, and competitive advantages. Basically, leverage brings about synergies in the new company. Leverage usually occurs through the customer/product matrix, strategy, talent and people flow, and reputation (Smallwood & Ulrich, 2002).

The customer/product matrix is one of the most common reasons large companies choose to acquire new or start-up companies. It’s often easier, and sometimes more cost effective, to keep up with technology and achieve new product growth through acquisitions than through research and development. At the same time, when merging or acquiring, a company not only acquires the products of the target company, but potentially its customers as well. The trick then becomes convincing all of the combined
company's customers not only to continue to buy from the new company, but also to buy new products acquired through the merger.

Strategy plays into leverage in that the combined company must decide which business units it wants to continue, and which it should sell in order to generate revenue for the company. It's important that the company have a corporate-level strategy that makes sense and that it sticks to it. For many combined companies this may mean divesting business units in order to focus on core competencies and not become too diversified, a problem that causes the downfall of many well-meaning companies.

Consistent with the corporate-level strategy is determining where employees fit in the new company. Many of the reasons firms are successful in the first place are because of the people working in the firm. The idea that two heads are better than one supports that talent and people flow add to a merged company's leverage. However, it is important that the combined company retain the same talented people that initially contributed to its success. Another people factor contributing to leverage is the concept that new ideas are formed by combining people, which add to leverage. For example, employees can share information regarding processes, procedures, markets, technology, etc, and form new and wonderful ideas.

Finally, if the acquiring company has a good reputation, that reputation will (hopefully) follow the new company. Thus, products that haven't sold well under its first label may do better under a new brand name. Also, it's possible if the brand is strong enough that some products can now be sold at a premium and still maintain market share.

Although merging or acquiring in order to obtain efficiency and leverage sounds like a good idea on paper, mergers aren't as easy as they seem. The reasons behind
mergers aren’t always clear cut either. Many times there are other factors that cause CEOs and top management to consider a merger or acquisition, such as pressure from shareholders to perform in the short-term or the desire to be the “biggest and the best” (Smallwood & Ulrich, 2002). Reasons like these often result in ill-researched and hasty mergers and acquisitions.

**Other Factors Resulting in Mergers**

Most companies merge because they think it will result in efficiency and leverage. The company suddenly has a greater market share while making a higher profit. What could be better? However, the fact is that many companies that go through a merger or acquisition have overestimated the benefits involved and underestimated the costs. In addition, companies pay too much for target companies based on these erroneous estimations (Henry, 2002). Companies make these mistakes largely for three reasons: inexperience of the acquirers, pressure on the CEO, and lack of input from the board of directors (Levinsohn, 2002).

For companies that frequently acquire other companies, knowing what to look for and evaluate in a deal becomes commonplace. However, for companies who haven’t pursued this strategy before, they often have only the word of their investment bankers to follow. The inexperience of management often causes problems because they haven’t chosen to merge with a company that is a good fit, they haven’t developed a business strategy for the combined company, and they don’t know which areas to evaluate to determine a fair price.
Another factor that may have detrimental effects on a merger or acquisition is if the CEO and top management are under short-term pressure to perform. A merger or acquisition may be seen as a “quick fix”; now the company will have the technology it needs or the most popular product on the market. However, acquiring a company doesn’t rid the company of past problems, and usually makes even more problems. For example, if a company is under-performing due to poor management, acquiring a successful company only means that the poor-performing managers now have more opportunities to loose more money. It’s easy for management to get caught up in the excitement of merging when they’re being pressured to make the company perform better.

Finally, companies’ boards of directors usually aren’t very involved in the decisions companies make, and deciding to merge with or acquire another company is no exception. Too often it’s easier for boards of directors to agree with whatever the CEO and management present rather than questioning the decision, or doing research themselves. After the recent Enron scandal, more boards are taking an active role in their companies, which will hopefully extend towards companies’ decisions to merge (Levinsohn, 2002).

**Reasons Mergers Fail, and Suggestions to Help them Succeed**

**Financial Reasons**

It has been mentioned that most mergers and acquisitions fail, and that one of the major reasons is because companies overestimate benefits and underestimate costs. It has also been mentioned that management and the board of directors can be held directly
responsible for these mistakes. The question now becomes, “How did they manage to make these mistakes in the first place?”

Although it may seem a simple equation to determine if a merger will increase value (the inflows of value made by merging must exceed the outflows of value made by merging), determining what the inflows and outflows are, as well as their value, is tricky. Inflows consist of two areas: the value of the acquired company, and the value of synergies formed between the joined companies. Consequently, there are three more categories of outflows than inflows. These categories are the acquired company’s value (if the value estimated is more than the actual value), the premium offered in the acquisition, transaction costs, restructuring costs, and value leakage (Schweiger, 2002).

The value of the acquired company is based on the cash-flows generated by that company. Another factor in determining the value stems from the risk associated with the company. The acquiring firm can only estimate what the future cash flow of the acquired company will be. This is hard, because besides the acquiring company making an assessment, it also has the market’s opinion and the management of the target company’s opinion influencing the actual value (Schweiger, 2002).

As mentioned earlier, one of the reasons companies choose to merge is because they feel the synergies achieved in combining the two companies will save costs and generate revenues. However, also as mentioned earlier, this is easier said than done. The trick is not only to estimate the money flow from achieved synergies, but also the probability that the synergies will be successfully implemented.

The first outflow associated with a merger or acquisition is obviously the price the acquiring company pays for the target. This price is largely determined by what the
acquiring company decides the actual value of the target company is, which, ironically, is also an aspect of cash inflow (Schweiger, 2002).

However, the part of the acquisition price that usually gets acquirers in trouble is the acquisition premium. This is the price paid to the target company above what the company's actual worth is. The purpose of this premium is simply to convince the target company to sell. It is important that the premium price isn't above what the newly combined company can reasonably achieve in revenue in a realistic time period.

Other big costs are those that come about from simply going through with the merger or acquisition. The two major costs here are transaction costs and restructuring costs. The transaction costs are costs associated with achieving the merger, for example, the costs of doing research on the target company and fees paid to professionals consulting on the merger. The restructuring costs include anything the newly combined company has to do to organize the company so it's able to achieve predicted synergies (Schweiger, 2002).

The last source of value outflow is value leakage. Value leakage is caused by two situations. The first situation is if merging actually causes a negative impact on the intrinsic value of the combined firm. This could occur if the merger causes a reduction of productivity, a loss of sales, or a loss of key employees, among others. The second situation in which value leakage could occur is if there is some kind of negative change in the environment, such as a downturn in the economy, while the merger is taking place.

Generally, to insure that the inflows of value are greater then the outflows of value when a merger is taking place, the companies need to make sure they estimate, as realistically as possible, both the inflow and outflows of value, keeping in mind that
management usually overestimates inflows and underestimates outflows. After the companies have reasonable estimates on both, then they can determine if the merger is actually a good idea (Schweiger, 2002).

Cultural Reasons

However, value inflow and outflow is not the only reason that mergers fail. According to an article in Human Resource Planning, “a Forbes survey of 500 CFOs found that the top reasons why mergers failed were not financial issues, but people-related issues: incompatible cultures, inability to manage the acquired company, inability to implement the change, synergy overestimated, failure to forecast foreseeable events, or clashing management styles or egos” (Price & Walker, 2000).

Corporate culture is a major consideration in these “people-related issues.” In fact, it is estimated that 85 percent of failed mergers fail due to cultural problems (Miller, 2000). Corporate culture is “the set of shared, taken-for-granted implicit assumptions that a group holds and that determines how it perceives, thinks about and reacts to its various environments” (Kreitner & Kinicki, 2001). Corporate culture guides the way things are done in a company, including the way internal and external customers are treated, how decisions are made, how formal the company is, and what values the company advocates and demonstrates (Miller, 2000).

Corporate culture serves four functions within the organization. The first function it serves is to give organization members an organizational identity. The second function is to facilitate collective commitment of the employees towards their organization. Corporate culture also promotes social system stability, which takes into consideration
how conflict is managed within the organization and whether the organization’s overall environment is viewed as positive and supportive. Finally, corporate culture helps employees to make sense of their surroundings. In other words, it helps employees determine where the company wants to go, why it wants to go there, and how it plans on achieving its destination (Kreitner & Kinicki, 2001).

Given these definitions of corporate culture, it is easy to see how clashing corporate cultures can have a detrimental effect on a merger or acquisition. A metaphor by Kilmann et al., quoted by Katinka Bijlsma-Frankema in the Journal of European Industrial Training, may help visualize why corporate culture can be a problem:

Picture two icebergs in the ocean, where the tip of each represents the top management groups - primarily financial people - deciding the fate of the two companies and how the merger will work. As these top management groups set the merger in process, the woe icebergs begin moving toward one another until the tips meet and mesh as one. Such a consolidation however, can never take place. As the icebergs approach one another, it is not the tops that meet; rather it is the much larger mass below the surface of the water, the respective cultures that collide. Instead of synergy there is a culture clash (Bijlsma-Frankema, 2001).

This often occurs when there is poor integration of culture within a merger. Although it is sometimes feasible for the dominant company’s culture to encompass the acquired company, or for the companies’ cultures to remain separate, these are not the norm. Often times a new culture will emerge as the merging companies integrate. Furthermore, many merging companies elect to form a new culture.
However, redefining company culture to encompass joint missions and values, as well as convincing all employees it’s the right thing to do is no easy task. As Tony Williams, COO of Pillowtex, a company made of three separate divisions and recently emerging from bankruptcy, says, “The real trick, the real success, will be whether we have been able to change the company, the culture. That’s the really hard part. All the other stuff...you can pull out of a textbook” (qtd. in Hogsett, 2002).

According to Smith, there are five steps to ensuring that conflicting corporate cultures aren’t the death of a merger or acquisitions. The first step is to do a cultural audit by reviewing the values, work ethics, leadership, structure, etc., of each of the companies. Using this information, it will be easier to identify possible problems in trying to merge the cultures, and thus, the companies (Smith, 2000).

The second step is to decide what the culture of the newly-merged company should be in order to support the new company’s strategy. Identifying what culture would help the new company succeed is critical. Some things to take into consideration are what values, work ethics, and leadership will aide the company in achieving its goals.

From this point, the third step is to determine how to get from the present cultures of the companies to the desired, combined culture. It is important that the company have a coordinated plan for making the changes needed to change the culture. Also, if the gap between where the companies’ cultures are and where the new company’s culture should be is too large, it is possible the cultural change isn’t feasible, making the success of the merger questionable.

Finally, steps four and five in changing culture are strategies for successfully implementing the change. Step four is a suggestion to form a cross-functional team to
help facilitate the change. Without every department having a voice in the change, it will be even harder to convince employees this is the right path to take, and they may resent management simply imposing this change on them without getting employee input. Step five suggests managing the change like a project, by giving delivery dates and monitoring progress as the plan continues. Without examining the results, the company will never know how the culture change is progressing, or if the plan needs revising in order to be successful (Smith, 2000).

Due Diligence

As mentioned earlier, one way to ensure corporate culture isn’t a problem in merging companies is to do a cultural audit, commonly called cultural due diligence. Due diligence is the extensive evaluation the acquiring firm does on the target firm before deciding to merge (Hitt, Ireland, Hoskinsson, 2003). According to Dillavou, “An effective due diligence process will confirm strategy assumptions and the fair price for the target and identify operational, legal, financial and significant merger integration opportunities and issues that must be addressed in evaluating the transaction” (Dillavou, 2002). Also, due diligence can identify if the success of a merger is so questionable that the companies may decide to back out of the deal, before wasting any more valuable time and money.

However, sometimes due diligence is done so poorly that the acquiring company ends up paying too much for the target company, an action that easily leads to a newly merged company’s failure (Hitt, Ireland, Hoskinsson, 2003). Dillavou suggests some tips
for conducting an effective due diligence, including the importance of including an
evaluation of the culture.

First, the team conducting the due diligence must be well versed in the
companies' reasons for merging and their future strategy. In doing this, the team can be
sure to evaluate important areas and information critical to the strategy of the merged
company. Similarly, it's important the due diligence team be aware of the target
company's current strategy to see if it will be easily integrated into the new company's
strategy.

It is also important that due diligence be thorough. This means not only looking
at financial and accounting records, but going a step further, for example, looking at tax
records. It is also important that the due diligence team identify any possible problems
from information they uncover, for example, if there are any business dealings that seem
shady or may have future legal implications.

Finally, due diligence should aid in integration planning. It is here that corporate
culture should be taken into account. Basically, the information learned in the due
diligence process should be considered when planning the integration process. In
addition to identifying possible problem situations, the due diligence process can also
identify areas where synergies may exist that that haven't been thought of yet (Dillavou,
2002).

However, looking only at financial reports, cultural differences, and conducting
due diligence won't achieve a successful merger or acquisition. There are still many
more pieces of the puzzle that need to be put into place. Many of these pieces can be
found in the Human Resource Department.
Human Resource’s Role in Mergers and Acquisitions

Get Involved Early

A recurring viewpoint from HR professionals is that the Human Resource Department needs to be involved in the merger or acquisition while it is still in the early stages. The main reason for this is because Human Resource professionals commonly think of areas that need to be addressed in considering the merger that other managers don’t think of. As Jeffrey A. Schmidt, a managing director of Towers Perrin says,” HR must have a seat at the planning table - that is, be involved at the beginning stages of a deal – to provide management with critical insights into how the merger or acquisition will affect the newly formed company’s people” (qtd. in McLeod, 2001).

Due Diligence

One way HR can be involved in the early stages of a merger is to include it in the due diligence process. There are two areas where Human Resource professionals can aid in performing a due diligence: in people-related issues and in cultural issues.

The people-related issues basically deal with any area that employees are going to be concerned with if the merger takes place. Some of these issues include retirement funding; health insurance benefits; other employee benefits; compensation systems, including stock options, salaries, and commissions; union relationships; outstanding employee litigation, such as law suites or workers’ compensation claims; employment contract; and seniority (Price & Walker, 2000; Bramson, 2000; Culture, 2001).

Besides people-related issues, cultural issues are equally, if not more, important in reviewing in the due diligence process. The importance of culture in a merger or
acquisition, as well as the need for a cultural audit has already been explained. However, it’s important to realize why Human Resource professionals come into play during this essential step. As Jeffrey A. Schmidt says, “they (companies’ management) don’t consider cultural issues early in discussions. . . . These mistakes will eventually come back to haunt the new company and its management” (qtd. in McLeod, 2001).

Thus, it’s up to Human Resources to consider the cultural implications in a merger. First, HR must understand the culture of both companies. To do this, it’s important that HR look at all aspects of the company that may have influence on their cultures. By borrowing an idea Hewlett-Packard and Compaq had while merging, forming an integration team made up of HR professionals from each company and keeping them separated from professionals in their own company, would ensure a fair and accurate portrayal of each company’s culture (Business, 2002).

Some important cultural factors these HR professionals should consider are the companies’ histories, locations, reputations, and products and services. HR must also look at power in the company, including who has it and how it’s used. This will affect how the company is managed, how employees are treated, and how employees react to management. Power also affects employees’ feelings about the company and its management, which are also important factors to consider when looking at culture.

Due diligence of culture also includes accessing things that may not seem important, but really are when considering employees’ feelings toward the company. For example, the dress codes of each company should be reviewed, as well as typical working hours and the physical facilities employees are working in. Also, HR should look at what each company’s management’s perceptions are for what the new company will look like;
what each company will bring to the table and how the new company is going to be run (Bramson, 2000).

Integration

After due diligence of people-related issues and culture is finished, and sometimes even while it’s still in progress, Human Resources’ job continues. HR also has an integral part in the integration phase of the merger. It’s important that HR is involved in integration planning, in determining how to retain key employees, and in aligning the new organization.

Integrating two companies can be hard and time-consuming work. That is why using a team to lead integration is usually a good idea. These teams can be formed early on, even before the merger is finalized, to aid in the due diligence process by determining whether integration between the two companies is even feasible. However, HR still plays a role in the integration process by first determining who the right people are to be involved in the team, and then by overseeing the team and making sure it is accomplishing the companies’ goals in a timely manner.

First it is important that the team be filled with flexible, creative, and energetic people. These people should be given the proper resources and authority to be able to do what they feel is necessary for the integration of the merging companies to work properly. Also, the people in the team need to be allowed to devote all of their time and energy towards the integration project. Thus, pulling these people completely from their ordinary jobs and responsibilities would be a good idea, if possible.
Once the team is created, it’s an integral part of HR’s job to oversee the team, either by being a supervisor, or having members of HR serve on the team. HR can set objectives for the integration team, and then ensure the objectives are met. HR can also ensure that the team is working efficiently and quickly. Also, if it seems the team isn’t accomplishing what it should be, HR has the autonomy to change the path integration should take in order to make it successful (Bramson, 2000; Price & Walker, 2000).

A primary responsibility HR has during the integration phase is to retain key employees. The first step in retaining key employees is determining who the key employees are. Walker & Price suggest following a series of steps to accomplish retaining key employees, the first three dealing with determining who the key employees are.

The first step is to “Define the future roles of executives in both merger partners” (Price & Walker, 2000). This is an important step because key employees may not always be top executives. Secondly, HR needs to “Define the management capabilities required for the future success of the business” (Price & Walker, 2000). And third, HR needs to “Identify the individuals who will be critical and any capability gaps that will need to be filled” (Price & Walker, 2000).

After key employees are determined, HR then has the challenge of deciding how to retain these employees. Bramson suggests first that Human Resource professionals ask the question, “How Long?” to determine how long these employees will continue to be key employees. It is possible that some employees are needed only through the merger, and then won’t be needed any more. For this reason, each key employee should be evaluated on their longevity of usefulness, and an appropriate retention plan be
designed for each individual (Bramson, 2000). In designing each key employee’s specific retention plan, HR professionals will be following Walker & Price’s fourth step by “Determining the actions required to retain key individuals through the merger” (Price & Walker, 2000).

Finally, HR also needs to assist in deciding how to correctly align the newly merged company. Alignment entails analyzing the infrastructure of business units, determining what resources are required to make this section of the company successful, and re-organizing resources so that each business unit is properly equipped to achieve its mission.

Because the success of a merger will partially rely on the synergies formed by merging, it’s important that any realignment of the merged company be efficient and effective. In doing so, HR must look at the future of the company, what resources, human or otherwise, will be needed, and then address any potential gaps. Also, it’s important that the alignment of the company, whether it is in people-related systems, or other processes, be consistent with the new company’s business strategy and ultimate mission. If Human Resource professionals ever needed a chance to prove their value to the company, helping a newly merged company correctly align its business is a perfect opportunity (Price & Walker, 2000).

Communication

However, the responsibilities of a HR professional aren’t only for the company to succeed in the merger, but also for the employees to feel comfortable with the merger. The main way this is accomplished is through communication. Communication to
employees regarding the merger can best be discussed using a series of questions: When to communicate? What kind of communication to use?, and How much to communicate?

In answer to the “when?” question, it is important that employees are informed of the merger or acquisition early on. However, it makes no sense for management to announce the merger if it isn’t prepared to answer at least some of employees’ questions. The sooner employees’ fears are calmed, the sooner they’ll be able to accept the merger and adapt to the pending change. It’s also important that management be truthful with employees at this stage and answers any questions it is unsure of by saying, “We don’t know” instead of misrepresenting the situation (Whalen, 2002; Price & Walker, 2000).

Many sources agree that all types of communication should be used when explaining to employees the ins and outs of a merger or acquisition. Also, this information should be repeated again and again to ensure that the message is being both heard and understood (Branson, 2000). However, it has also been found through research that informal communication has a bigger impact on the success of a merger then does formal communication (Whalen, 2002). This is also consistent with the idea that employees need to be able to express their questions and concerns, which often come about through informal communication channels in which upward communication is allowed (Bramson, 2000).

This is not to say that formal communication isn’t important, because it is. Formal communication should be accompanied by informal communication. In fact, research finds that formal communication is seen by employees as being more credible if the employee has first gotten to participate in some sort of informal communication with management and co-workers (Whalen, 2002).
How much employees should be communicated depends on the motive for the merger. According to an article in *Communication World*, “15 to 25 percent (of mergers) don’t require a lot of integration, because the merging units are dissimilar and there is no strategic value in consolidating them. Firms in this situation sometimes err by over-communicating to their employees” (Merger, 2002). This type of merger is consistent with a “financial synergy motive,” in which communication to employees should be minimal.

With an “operating synergy motive” however, companies may be intimately integrating all aspects of their businesses, including facilities and jobs. In situations like these employees have more fears and doubts because they are affected directly. In these types of mergers it is important to establish strong communication links between management and employees (Whalen, 2002).

Finally, as with anything else in a merger or acquisitions, the results of the communication strategies being used need to be monitored and evaluated. Basically, Human Resource professionals need to determine if what employees are being communicated is accomplishing managements’ goals. If employees still have a lot of questions or concerns, HR needs to know about them so a better communication strategy can be developed. When employees are properly informed, they will be more supportive of the merger or acquisition (Merger, 2002).

Although communication is a key factor in making mergers successful, it is only one of the factors. As Whalen states, “communication represents a critical element in all mergers and acquisitions, but it cannot create synergy where none exists or where cultures are incompatible. Nor can communication make up for laziness in the due
diligence process, poor initial planning or lack of understanding of how both firms add value to their customers" (Whalen, 2002).

Although it’s easy to speculate about what makes mergers and acquisitions successful or not, it’s easier to see how the proper steps (or lack there of) actually helps mergers succeed. Following are two case studies, one on the disastrous AOL Time Warner merger, and one on the possibly successful Hewlett-Packard Compaq merger. In studying these two mergers, it’s easy to tell why Human Resources should be involved in mergers and acquisitions.

Case Studies

AOL Time Warner

Announced on Jan. 10, 2000, the $350 billion marriage between America Online and Time Warner intended to integrate old and new media while increasing profits 30%. Instead, their strategy never materialized and stockholders lost a combined $280 billion in stock value (Roberts, 2002). Identified problems resulting in this financial fiasco can be attributed to poor estimation of financial gains from the merger, as well as improper evaluation of key HR issues.

The first problem with this merger is obviously that financial synergies were overestimated. The companies’ plan of “cutting costs and pulling together the diverse income streams at its disposal” (Crunch, 2001) obviously didn’t pan out as expected. Furthermore, AOL’s financial well-being was hit by the fall of the dotcom companies. In fact, AOL’s stock price was already dropping at the time the merger was finalized (Roberts, 2002).
The second problem with the AOL Time Warner merger is that they failed to analyze key HR issues appropriately. Although AOL Time Warner had a HR transition team in place at the beginning of the merger, they didn’t seem to focus on, and then implement any of the key issues, such as corporate culture and definition of executives’ roles.

AOL and Time Warner had very different corporate cultures. AOL had a culture of teamwork and constant change, as well as a top-down management style. Time Warner, being made up of many independent companies, had a slower and de-centralized culture, as well as having an improvisational management approach (Crunch, 2001), (Adams, 2002).

However, AOL Time Warner’s HR department seemed to be unconcerned with these cultural differences. In fact, “At AOL Time Warner, executives say the best way to dodge fatal missteps is to avoid altering the cultures in the first place” (Adams, 2002). Julian Kaufmann, an HR professional at AOL Time Warner went on to say, “One of the stupidest things you can do is to try to tell organizations that they can’t have their own culture” (qtd. in Adams, 2002).

As mentioned earlier, some merging companies can be successful by retaining their own cultures; however, this usually works best when the merging companies are primarily staying independent of one another. In AOL Time Warner’s case, the entire intent of the merger was to integrate their products and services, resulting in frequent communication between the two companies’ employees.

However, the biggest mistake AOL Time Warner made in “ignoring” the cultural differences was in failing to recognize that these cultural differences were also present in
top management, people who were required to work closely before, during, and after the merger. For example, Time Warner’s chief contact with Wall Street analysts, Joan Nicolais, rejected the 30% profit increase estimation AOL’s people came up with, declaring it was too high and that they could never achieve so high of a profit increase in such a short time period. However, she wasn’t listened to, and in the end, was right (Roberts, 2002).

Other key players in the merger also had cultural differences that resulted in conflict. Gerald Levin, Time Warner’s CEO and Steve Case, AOL’s chairman, had very different views of the way the new company should be run. When AOL Time Warner was considering acquiring AT&T’s cable company, Levin apparently pursued the acquisition without speaking with Case, saying he “hadn’t liked Jerry’s approach” (qtd. in Roberts, 2002).

HR could have helped alleviate this problem. If a proper cultural due diligence had been conducted, it would have been determined early on that these two leaders had management styles that didn’t mesh. This knowledge could have led to more defined job descriptions for the two men, re-evaluating who should be in leadership roles at AOL Time Warner, or maybe even scrapping the entire merger due to the cultural conflicts reaching all the way up the ladder.

Another Human Resources failure also dealt with top executives. Their roles within the new company weren’t specified before the merger, resulting in power struggles. The most noted power struggle was between Levin and Case. Although it was known that Levin would be CEO, and Case would remain chairman of the board, Levine
was worried about giving Case too much power. Although they came up with a solution, their relationship continued to be rocky (Roberts, 2002).

Power struggles also emerged between co-COOs Richard Parsons and Bob Pittman. AOL executives reportedly disliked Parsons (who originally was an employee of Time Warner) and talked about him behind his back. Pittman also made it widely known that he would like to be higher in the ranks of AOL Time Warner, and didn’t squelch rumors that he was the next CEO (Roberts, 2002).

Although Frederic H. Dickson, senior vice president of D.A. Davidson & Co. and observer of the AOL Time Warner merger commented, “The companies’ similar entrepreneurial styles have compensated for differences in culture and function, so we haven’t seen this mass exodus of key people that we’ve seen from other mergers” (qtd. in Adams, 2002), he’s been proven wrong. On December 5, 2001, Levin resigned as CEO. However, he spent time and energy to get Parsons promoted to CEO over Pittman. Pittman quit during the summer of 2002, after AOL’s accounting practices began being investigated by the SEC and Department of Justice, and AOL’s stock price plummeted (Roberts, 2002). Thus, not only did AOL Time Warner fail to define executives’ roles, it also failed to retain key executives.

Although it seems as if AOL Time Warner was aware that culture is often a relevant factor in mergers and acquisitions, executives chose to ignore it anyway. Thus, they’re paying the price, literally. Furthermore, AOL Time Warner has failed to retain key top management, and isn’t realizing the financial synergies it had hoped for. These problems could have potentially been avoided, either through better planning or by ceasing the merger, if the company had spent more time analyzing HR issues, as well as
financial issues, which really mattered to the success of the merger. Instead, AOL Time Warner is struggling to be profitable, much less successful.

Hewlett-Packard Compaq

Hewlett-Packard and Compaq had a very different, and more HR-involved approach to achieving their merger. Although it has not even been a year since Hewlett-Packard and Compaq merged, too early to determine if the merger was a success or not, results are looking as if this merger just might work. For example, at the end of fourth quarter last year, the “new” HP reported revenues of $18.05 billion, compared with the then-separate companies combined revenue of $18.17 billion a year earlier (Vijayan, 2002). Furthermore, HP has cut costs in two major business lines and has found cost savings by cutting headcount.

As the merger between HP and Compaq looks as it just might make it, the question now becomes “what did they do right?” The answer is simple: integration planning. Even before shareholders voted on whether the merger should take place, HP and Compaq had integration teams in place and over half a million man-hours of work poured into the integration effort (Business, 2002).

Unlike the AOL Time Warner merger, one of the first things HP and Compaq did was to choose who the leaders in the new company would be, and which business unit they would lead. HP Compaq’s reasoning behind this was that each leader could then be involved in the integration process for his or her business unit.

Human Resources also examined other people issues, such as retaining key employees. One way they combated this was to put into place a retention payment plan.
According to this plan, top executives would receive a payment of around three times their salary for staying with the company. Mid-level managers and other key employees would also be paid for sticking with HP Compaq, but only about half their salary (Raphael, 2002).

Another action HP and Compaq quickly implemented was to form an integration team, even before the merger was approved. This team, compiled of about 600 full-time employees, was named the “clean team” because, while the two companies were still competitors, this team had to remain separated from other employees from each company. Furthermore, each of the four main business units had its own integration teams, as did other key areas, such as Information Technology, Finance, and Human Resources (Business, 2002).

From the start, it was apparent to all involved that HP and Compaq had very different corporate cultures. While Compaq was described as a “go-getter,” HP was described as “stodgy” (Lashinsky, 2002). It was for this reason that the HR integration team performed a cultural due diligence consisting of 150 interviews of senior executives and 35 employee focus groups. The results: the cultures aren’t really that different when comparing divisions operating in the same product markets (Business, 2002).

However, there are differences that had to be dealt with. For example, HP employees utilized voice mail, while Compaq employees were e-mailers. Also, HP mulled over decisions, making sure it chose the right one. Compaq, on the other hand, made quick decisions (Business, 2002).

HP Compaq also believes in having good communication with both its employees and customers. When there was discussion about changing employee benefits after the
merger was finalized, Susan Bowick, Vice President of HP’s Human Resources said, “When we have changed benefit programs in the past we’ve thoroughly developed alternatives, agreed on the end goal and guiding principles, and communicated decisions well ahead of implementing them... This is how we will continue to handle any decisions around all HR programs going forward. Nobody will have to read about anything in the fine print of a proxy statement” (qtd. in Raphael, 2002).

Furthermore, the integration team also planned how to launch the new company to customers. A tool kit, including information about the combined company’s products was given to each sales representative to help them assist customers in understanding the new company (Business, 2002). Apparently this tactic worked, as InternetWeek reported that “More than half of end users said there’s been no change in their experiences after the companies merged” (Wagner, 2002). The reasons for this were said to be good communication and an organized sales force.

In general, HP and Compaq followed the guidelines outlined for achieving successful mergers, more specifically, those guidelines laid out for the Human Resources Department. First, HR was involved in the process early on, before the merger was even finalized. Second, an extensive cultural due diligence was performed. Third, integration teams were utilized and explored issues such as employee placement and post-merger retention. And finally, HP and Compaq laid out communication plans for letting both employees and customers know what is going on.
Comparison Chart between AOL Time Warner and HP Compaq

<table>
<thead>
<tr>
<th></th>
<th>Corporate Culture</th>
<th>Role Definition</th>
<th>Integration Team</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>AOL Time Warner</strong></td>
<td>knew there were differences, but decided each company should retain their own culture</td>
<td>developed talent profiles of 300 executives, but failed to define top management's roles early on, resulting in power struggles later</td>
<td>formed when merger plans were announced and determined which areas needed the most HR presence.</td>
</tr>
<tr>
<td><strong>HP Compaq</strong></td>
<td>conducted a cultural due diligence, determining where cultures were different, and if there were potential problems</td>
<td>decided early who the leaders would be in each business unit and developed a retention payment plan to reward executives for staying with the company during the merger</td>
<td>full-time integration teams were implemented even before the merger was finalized</td>
</tr>
</tbody>
</table>
Conclusion

In comparing the success of AOL Time Warner's merger and Hewlett-Packard Compaq's merger, it's easy to see who came out the winner. In comparing their merger strategies, including their focus on HR issues, it's also easy to see why mergers and acquisitions need to be analyzed well in advance and include due diligence, including cultural due diligence, integration planning, and analysis of HR issues, including communication and employee retention. If more companies who are considering merging with or acquiring another company would put as much time as they do money into the merger, and analyze some of the key people-related issues, more mergers would have the fighting chance HP Compaq achieved.
Bibliography


