

MANAGING RISKS IN THE MERGER & ACQUISITION PROCESS BY IT COMPANIES

Full paper

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Abstract: A practical and real case of Merger and Acquisition of two IT companies is presented in the paper as a project, with the qualitative and quantitative analysis of the risks that could occur in such unique endeavor. Theory fundamentals are discussed as an important knowledge for such analysis. According to the results of the analysis a Risk register is filled-up as a basis for Risk Management Planning activities in M&A project.

Key words: IT Business, Merger & Acquisition, Risk Management, Risk register.

1. INTRODUCTION

In the new economic and business environment the IT companies are faced with dynamic changes and development policies. In that sense, Mergers and Acquisition (M&A) have been a powerful tool for companies to implement their business vision and strategy. The tool has been used for various purposes, such as: when company wants to expand on new markets, to extend portfolio of products or services, increase headcount of the company and many other goals. With Acquisitions a company can perform a hostile takeover, but also in history there have been friendly Acquisitions and Mergers of companies for achieving higher goal. Whichever the strategy is, the M&A is a tool through which a company can make investment in order to get future benefit. This investment comes with a risk, usually the higher the risk is - the higher the benefit may be. Sometimes it is a matter of existence for company and in order to survive on the market has to take some actions that in particular cases can make differentiation and create price or service or quality differentiation through Mergers or Acquisition.

The research about the M&A of the companies in IT sector, in order to make this process more effective and successful is very difficult due to the nature of the process.

Only successful stories are presented in a limited way. However in the theory [1], [2], [3], [4], [5] there are many approaches for how to implement M&A, what phases is the M&A consisted of. Which phase or step of the M&A takes precedence over the other and so on. There is no silver bullet that will make one Merger or Acquisition successful by following certain steps. Rather, there is experience and tailored process and phases according to the subject's evolution phase and knowledge. It M&A between two companies can be considered as a *project* since it is temporary endeavor that when completed creates unique product and/or service [8].

2. PROBLEM DEFINITION

In this contribution it is reviewed a case for Acquisition of IT companies working in different geographic regions with similar service offerings. The most common phases of M&A are going to be elaborated that should take place during the process itself, what each phase is consisted of, what is the input, output of it just to have clear view of the steps that one Company undertakes when considering or actually performing M&A. Since the M&A could be considered as a *project*, the Risk Management Process defined by PMI Institute [7], is going to be applied to the research of the M&A process by two real companies presented that could exist on the market. Each M&A is consisted of several phases, but in this research the **Integration** – as the most interesting and challenging phase has been selected for elaboration. However, the problem is how to make the process successful, so the Risk Management Process is applied for the Integration phase of M&A for IT companies. In the research, Risk Identification, Analysis and Response planning is conducted for each Department in the company in parallel, making possible the Risk Management Plan to be filled as Risk register, used in discussions and conclusions. Furthermore, the Cynefin framework, as potential decision making framework is used as tool that can be utilized during the process of M&A. The developed Risk register can be used as starting point in the *project* of M&A between the companies as case study.

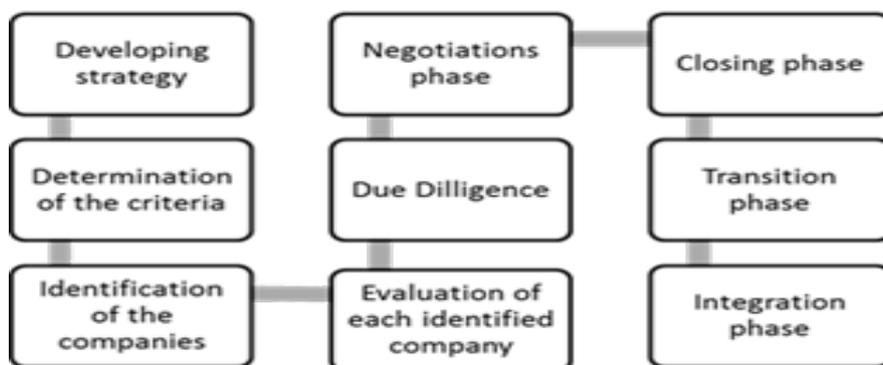


Fig. 1. Phases of the Q&A [6, 8]

To make analysis of the risks in the M&A process, the phases of the M&A should be clearly divided, making possibility to develop the criteria and planning the activities.

For risk management analysis the Data Flow in Risk plan is performed in accordance with the PMBOK [7].

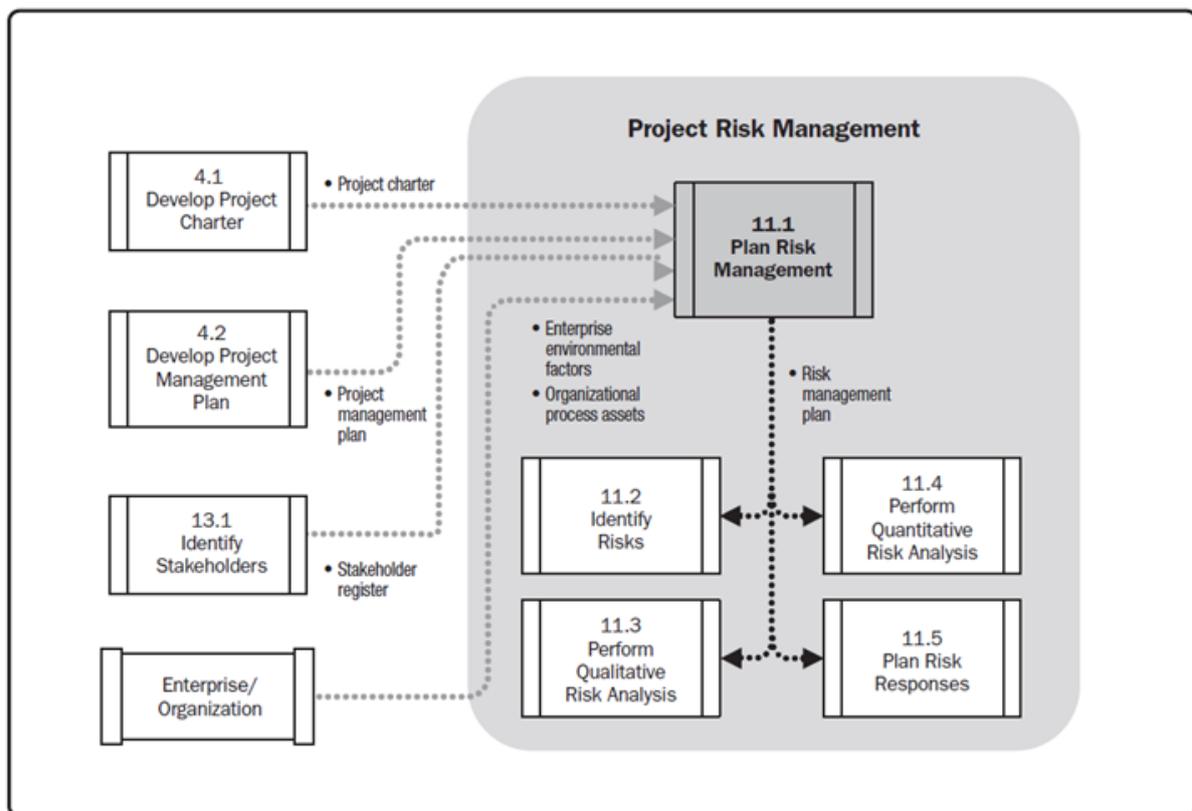


Fig. 2. Plan Risk Management Data Flow Diagram, PMBOK [7]

3. PROBLEM SOLUTION

To make the analysis complete, real and practical, a case study, elaborated in details [8], presented in this paper, involve two companies GAMA and DELTA. The assumption is that company GAMA passed all phases of the M&A process entering in the Due Diligence phase with the company DELTA and finished the Negotiations and Closing. Since DELTA is service IT company, there is no need for Transition phase. GAMA makes preparations for Integration phase. On the figures bellow both companies GAMA and DELTA are presented with their organizational charts. The main goal of the merge & acquisition for these two companies are that GAMA is going to buy smaller company DELTA that deals with the similar services as GAMA on its' particular geographical area, enabling GAMA to approach to the new markets. The strategy of GAMA is:

- Completely to acquire DELTA,
- To integrate DELTA in its' organizational structure,
- To optimize the used IT systems,
- To keep DELTA staff as much as possible,
- To takeover DELTA's clients, enabling its (GAMA) services to such clients,
- In two years - to enhance the number of workers that are working in DELTA's environment, for 50%.

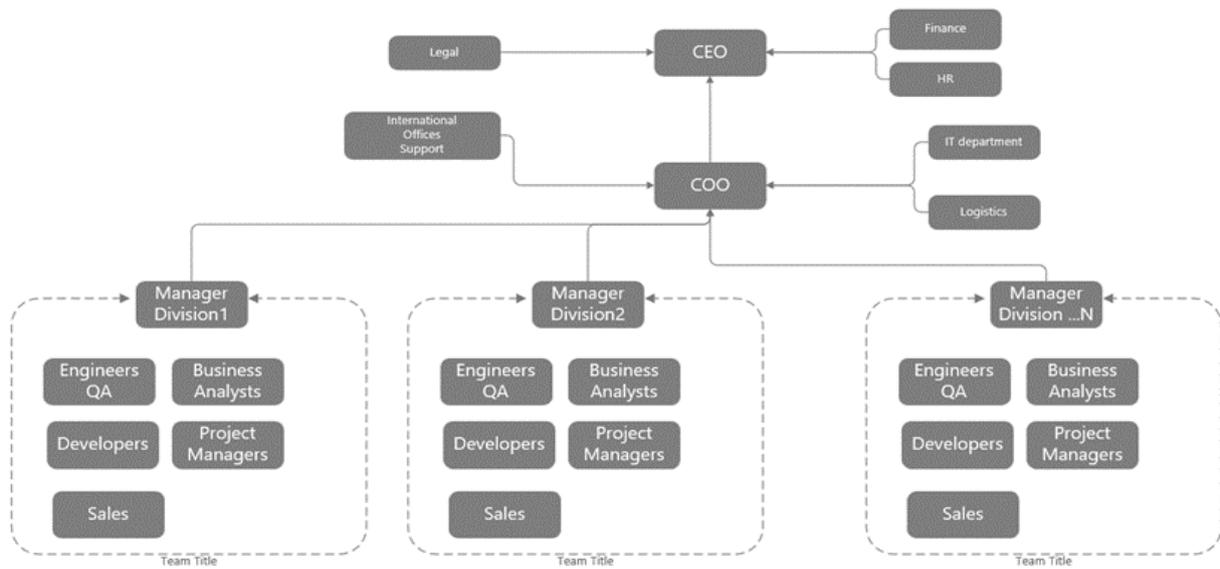


Fig. 3. Company GAMA

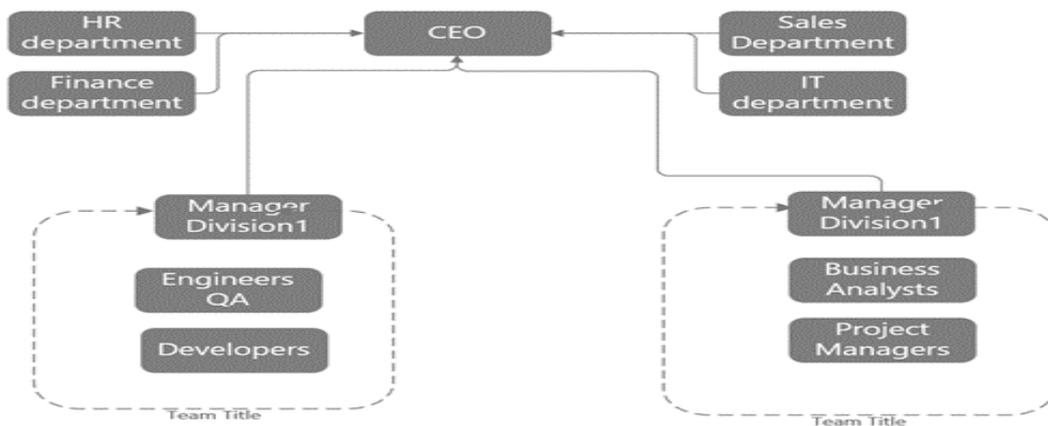


Fig. 4. Company DELTA

According to theory, to develop such strategy goals it is necessary to use common or adopt planning model for integration infrastructure [8], presented on Fig. 5. This plan includes forming a team that can create Integration plan to predict and overcome all risks, treats and obstacles. Only that way the strategy could be implemented successfully.

4. DESCUSION AND RESEARCH

For more effective M&A process Integration team should include representatives from GAMA and from DELTA and they have to make a good plan for activities undertaken for integration, considering all aspects that are relevant for both companies. Have a insight in the structure of the GAMA, in particular, one of the production' departments and if it is compared with the one of DELTA, presented on Fig. 6, below, it seems that they are quite different. GAMA has matrix organization, while DELTA is organized functionally.

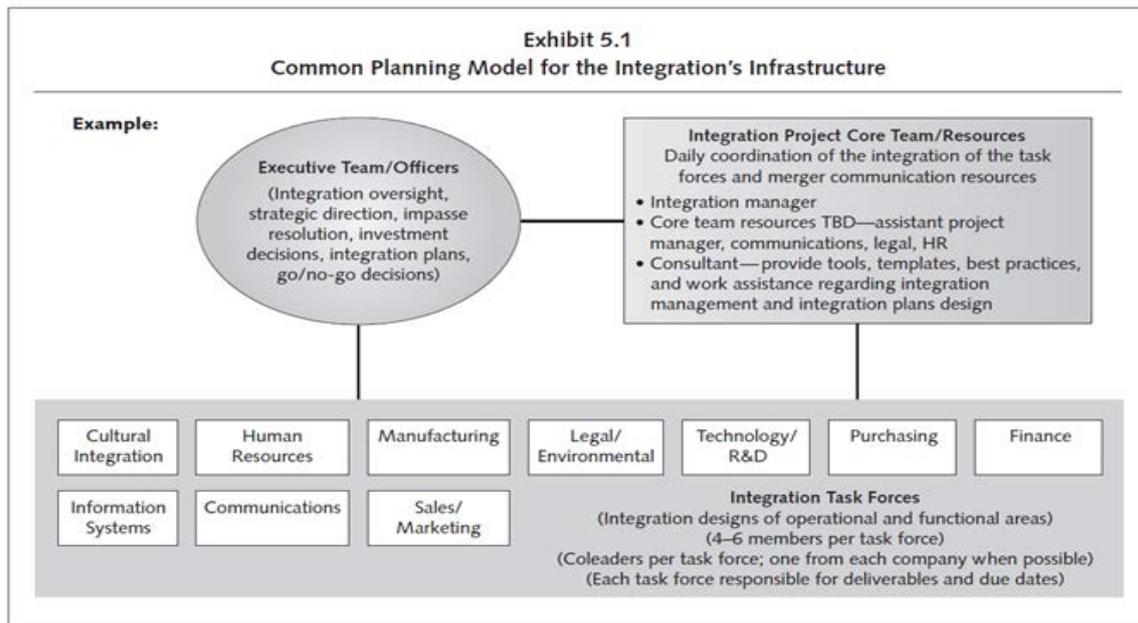


Fig. 5. Common Planning Model for the Integration's Infrastructure [2]

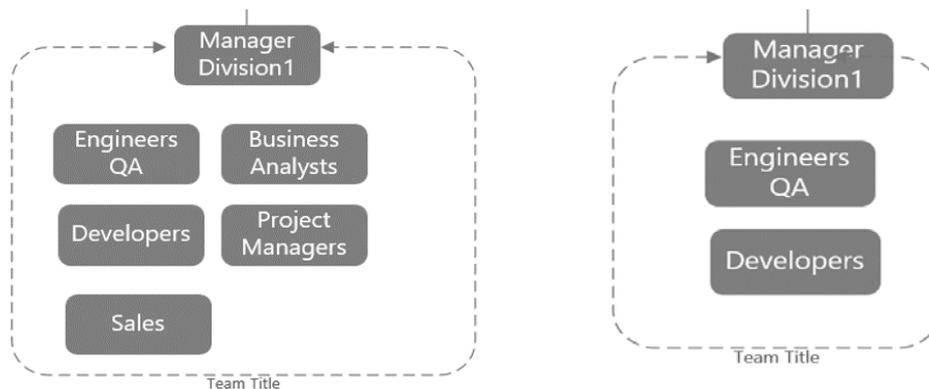


Fig. 6. Comparison of production departments of GAMA and DELTA

One potentially treat could be “How to re-organize production departments from both companies in one department” taking in account all differences and incompatibilities. Additionally, a serious treat could be the resistance of the workers for different reasons. As it is explained in [2] according to the analysis by Clemons, Thatcher and Row, the people could be grouped in three categories, or, as they named such categorization the “Resistance pyramid”. The basis of the pyramid are the people who don't have complete information about integration and the efforts that are needed, and they are “Not Knowing” people. In the middle are the people who can explore lack of skills and knowledge for the job in the company after integration, called “Not Able”. The last category are people who resist to integration, and those people are “Not Willing”. For each category/group of people in the pyramid, Integration team makes activities for response in order integration process to be effective and successful. The actions are presented on Fig. 7.

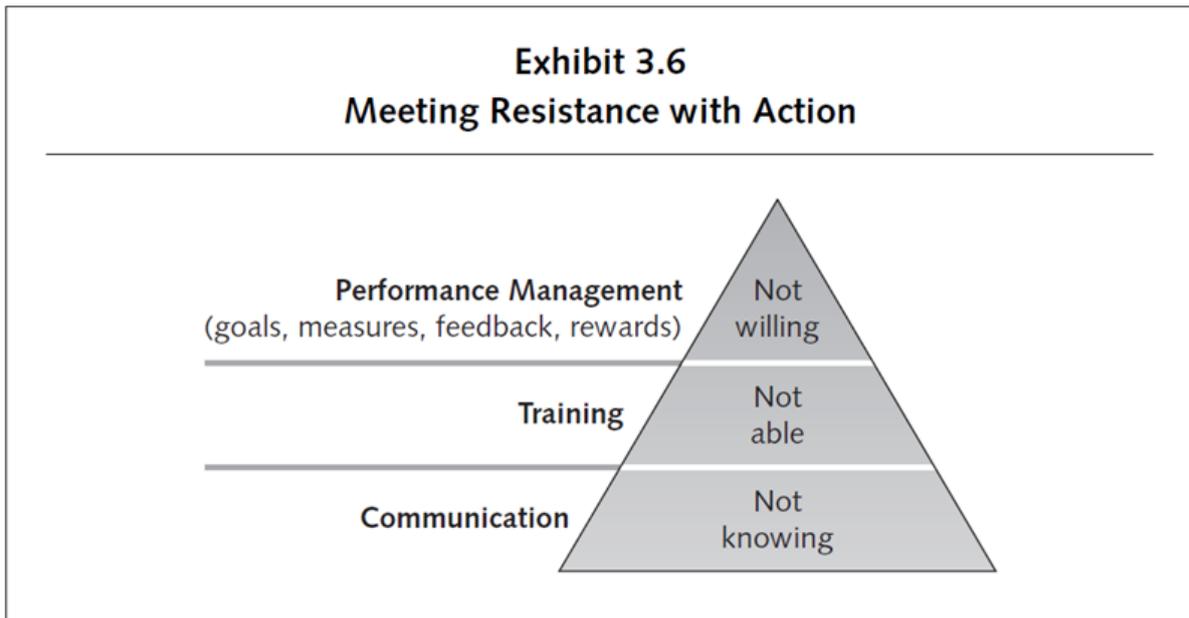


Fig. 6. Resistance pyramid and actions for each group, adopted from [2]

The presented treat is only a part of the possible treats that could occur and that are challenges for the Integration team. The project of M&A is not repetitive and reversible and is unique for the legal subjects in the process, so the team should consider all risk and make Risk Management Plan how to overcome such obstacles. In the Risk register some of identified and quantified risks are presented with a grade of importance for the process. The templates for this Risk register and Risk Management Plan are download from the eGovernment site of Tasmania project template documents, useful for use in this case (http://www.egovernment.tas.gov.au/project_management/supporting_resources/templates), issued under the license of the Creative Commons 4.0 (<https://creativecommons.org/licenses/by/4.0/legalcode>), having a possibility for changes and additions to the plan. Risk register presented below is only a part of a complete risk analysis investigated and developed in [8].

5. CONCLUSION

Merger and Acquisition is a very powerful tool or a possibility for company' strategy implementation. It could be used when company wants to approach to a particular market, to enhance the number of workers or services provided and in general to level-up their business portfolio. However, M&A as an investment like a project, lead to more profit or benefits with a risks that have to be managed in accordance to Risk Management Plan for the whole such project. Making the Risk Management Plan is very creative and not easy task, so a competent team should be created and to develop an action plan to overcome all obstacles and treats. Qualitative and quantitative risk analysis is needed to fill-up Risk register that is basis for implementation of successful M&A projects.

Table 1. Risk register for integration process of GAMA and DELTA companies (H-High, M-Medium, E-Extreme, IT- Information Technology department, Pr-Production department)

ID	Description	Impact	Category	Probability	Impact	Grade	Plan and Risk response actions(Avoidance, Transfer, Mitigation, Acceptance)
1	Not possible to integrate Active directory of the companies	Both companies are using different systems. One of the company uses internal Active Directory and the other company uses cloud services including cloud Active directory. Due to these differences there is a risk that it won't be possible to integrate these systems either new software will needed to be purchased that will enable federation of the systems.	IT	H	H	A	Mitigation. Invest in small research project to learn on possible ways to integrate these systems.
2	Increased number of licenses for particular applications as result of increased number of users on the existing systems as consequence of the Acquisition.	Need to increase number of available licenses for particular software thus increasing OPEX For example, we might need to purchase the next level of Jira licenses stage.	IT	M	H	B	Mitigation, adding users one by one in order to discover real need of users for accessing the systems requiring licenses. Optimizing current license usage among current users.
3	Lack of proper communication to the employees of Delta and not setting proper expectations during the acquisition	Due to lack of communication, or not appropriate communication a degradation of motivation of the employees or even increase of the churn rate of employees.	Pr	M	H	B	Mitigation, establish multiple channels of communication, organize polls to test the opinion of the employees. Creation of workgroups to establish proper communication channels.
4	Key employees departing due to dissatisfaction as result of levelling up the seniority and benefits.	Key employees with Intermediate level of knowledge may lose benefits when evaluated according to the Gamma's scale for seniority.	Pr	M	E	A	Mitigation, establishing communication with key employees of Delta and managing their expectations. Creation of additional level of seniority and/or benefits for these employees.
5	Delta employees might not follow established work processes as defined in Gamma.	There might be difference is the work processes, norms, code standards implementation, or expected quality outcome between Gamma and Delta that may influence on the quality delivered to the end customers.	Pr	H	M	B	Mitigation, Organization of technical trainings, presenting the processes, rules, code of conduct and the reward systems implemented in Gamma.

ID	Description	Impact	Category	Probability	Impact	Grade	Plan and Risk response actions(Avoidance, Transfer, Mitigation, Acceptance)
6	Decrease of quality delivered toward end customers during the M&A process.	As result of changes ongoing within the companies decrease of quality in the services delivered toward end customer may happen that will put in jeopardy continuity of the contract with some customers.	Pr	M	E	A	Mitigation. Establishing plan for collecting feedback more often and increased communication with the clients to enable early detection of possible issues. Implementation of system to individually handle employee that may be influenced by this acquisition.
7	Tools and Software used by the employees of Gama and Delta might not be compatible especially when working in a single team.	As lack of standardization in Delta some of the employees might use hardware or software that is not within the defined standards of Gama.	Pr	M	H	B	Mitigation. Creation of team to asses and list all the HW and SW used in Delta and do a comparison with the standard HW and SW used in Gama. Additionally, creation of transition plan on how the HW and SW is going to be updated or migrated.
8	Resignation by key employees from Delta	Resignation by key employees from Delta or the team leaders as result of various reasons (dissatisfaction, disagreement with the acquisition, not being able to integrate etc.) As a consequence, even more team members may follow the leads jeopardising service delivery quality and relationship with some of Delta's customers.	Pr	M	E	A	Mitigation. Involvement of the HR team through discussions with key employees and their line managers. Creation of personalized development plan. Inclusion of the key employees in the company organizational processes.

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