Integrating Acquisitions – Enterprise Maturity model

Sachin Chitlange, Ashwani Arora

Abstract:

Globalization has led to a sudden spurt in Mergers and Acquisitions over a past few years. Having a long term IT strategy in place beforehand helps alleviate lot of pain points associated with systems integration during Mergers. This paper illustrates how organizations can leverage and achieve the merger synergies for their ERP systems by following a simple Enterprise Maturity framework.
Integrating Acquisitions - Enterprise Maturity Model

Background

M & A's help companies grow and expand their footprints in multiple industries and geographies thereby ensuring that they stay on top. It is important to understand the basic concepts related to this phenomenon. The standard definitions used in industry for M & A are cited below.

The term merger involves combining of two or more entities resulting in continuation of one of the existing entities or forming of an entirely new entity.

When one or more entities merge with an existing entity, it is the case of absorption. *The merger of Novelis and Hindalco is such a case where the identity of Novelis is lost.*

Amalgamation involves cooperation and collaboration of two or more entities and forming of a new company like *Arcelor – Mittal.*

Acquisition is to seek effective control over the assets or management of the corporate without any combination of both of them like *Mahindra - Satyam computers.*

Though, the terms ‘merger’, ‘amalgamation’, ‘acquisition’ and ‘takeover’ have been specifically defined, they are generally used interchangeably.

M&As aim at optimum utilization of all available resources, achieving synergies in all areas, achieving economies of scale, forming a strong talent base, installing an integrated research and development base and ultimately improving the Profitability.

M&A Activity

The volume of worldwide mergers and acquisitions totaled US$941 billion with around 17000 numbers of announced deals during the first half of 2009 a decrease of 40.2% from 2008 totals and the lowest level for deal activity for an opening six month period since the first half of 2004. However, it is expected to pick up better than before by the start of 2010 as the market recovers from one of the worst ever recession.

Below figures provide M&A volumes by Industry and Geographies for the first half of 2009.

**Worldwide Announced M&A by Target Industry – Jan – Jun’09**
About this paper

IT integration as part of M&A is different from typical internal system integration projects because M&A Integration is riskier and needs to be done faster. However, many M&A initiatives may not deliver the expected outcome. Success of the IT integration stage immediately after the Merger can help build a positive impression on all stake holders to help achieve long term business goals.

As shown the diagram below, this article tries to highlight a basic / high level maturity model for Integrating ERP Applications, during Mergers and Acquisitions.

The paper also tries highlighting the major challenges and key success factors in an M&A to ensure that the expected outcome is realized, followed by a case study.
M&A - Practical Challenges faced during Transition

Key Pain Points

- Know How
- Customizations
- Cost of Transition
- Time-To-Market
- Compliance Lapses
- Adverse Change Impact

Potential Failure Modes

- Few companies have a comprehensive methodology or the experience to execute technology dimensions of M&A
- Result in Low source data Quality, home-grown applications and workbooks result in Gaps or missed conversions, inconsistencies
- Lack of detailed technology fit-gap assessment
- Cost impacts from interdependent projects are rarely accounted for
- Estimated schedule for transition is usually based on insufficient facts
- Low experience of what needs to be done, how to do and what it would take
- No plan for Application or Information Risk management, Requirements for retaining historical data/ record keeping or Reporting requirements
- Inadvertent or unanticipated technology impacts to the legacy employees
- No communication, training or adoption plan for Technology Change

Application Maturity Model – IT Integration in M&A projects

Typical transition for Merger between large banks/FIs spans around 18-24 months and IT changes would be involved in all the stages. Transition would include Due Diligence, Planning and Execution phases. Due diligence and Planning phases are most critical because of the speed at which M&As need to be integrated. These phases determine the level of integration, applications that need to be retained/ retired and data storage requirements to meet the business objective of M&A.

The diagram below represents a phased approach to such kind of large IT Integration projects.

Application Maturity Model – IT Integration in M&A projects
Companies which have M&A as a part of the growth strategy plan ahead of time and build a framework for Systems integrations during acquisitions. The strategy goes hand in hand with the systems capabilities/ Infrastructure scalability available with the company. Though systems scalability is not a deciding factor for Merger, a good understanding of the same upfront would help in making an informed judgment of the likely systems impact.

Every stage above has been further elaborated with the details of exact IT and Business objectives that need to be achieved

### Application Maturity Model – M&A projects

<table>
<thead>
<tr>
<th>Focus: Data Integration</th>
<th>Focus: Process Integration</th>
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</thead>
<tbody>
<tr>
<td><strong>Stage 1a</strong></td>
<td><strong>Stage 1b</strong></td>
</tr>
<tr>
<td>Legal Day 1 Manual Data Consolidation</td>
<td>ETL Stage Temporary Data Extracts</td>
</tr>
</tbody>
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<table>
<thead>
<tr>
<th><strong>Stage 2</strong></th>
<th><strong>Stage 3</strong></th>
<th><strong>Stage 4</strong></th>
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</thead>
<tbody>
<tr>
<td>Interface Stage Business Process and Data Integration</td>
<td>One Apps Centre of Excellence</td>
<td>Best Practice Best of breed processes / Apps</td>
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### Business Objectives

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<tr>
<td><strong>Consolidated Statutory Reporting for the interim period</strong></td>
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<td><strong>Support Business processes by moving toward common Data pool</strong></td>
</tr>
<tr>
<td><strong>Business Process Integration and Application Rationalization</strong></td>
<td><strong>Business Process Integration with continuous improvement</strong></td>
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### IT Objectives

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<tr>
<td>Integrate data quickly to meet mandatory reporting requirements via manual effort</td>
<td>Integrate data quickly to meet mandatory reporting requirements via a small/medium scale data-warehouse implementation</td>
<td>Integrate master and transaction data to support real time business processes</td>
<td>Integrate application modules with a goal of keeping the business functionality in the system that supports it best (“center of excellence”)</td>
<td>Implement the core system / processes of the acquiring company in the acquired company.</td>
</tr>
<tr>
<td>E.g. Using Global Consolidation feature of Oracle ERP to consolidate data in GL</td>
<td>E.g. Writing ETL queries to extract data in single data warehouse to support Balance Sheet Annexure</td>
<td>E.g. Use of Interfaces to integrate data from multiple product system to Oracle GL. Merge COA, Supplier or Customer Data</td>
<td>E.g. Integrate sub ledgers for business processes, Integrate business functions like Approvals</td>
<td>E.g. Implement best of breed processes to maintain competitive edge in the industry</td>
</tr>
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</table>

The above approach clearly suggests that:

- Initial focus has to be on Data Integration and as the Merger matures the IT project has to focus on Process Integration to achieve synergies
- Clear deliverables need to be identified at each stage to make the model very objective, Refer Fig. below for sample deliverables
- Clear Entry - Exit criteria’s need to be defined at each stage
Sample Milestones / Deliverables at Each Stage

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What are the Key success metrics at each stage?

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- Speed of project implementation using simple work around OR standard functionality to consolidate data
- Accuracy of reports
- Speed of project implementation to extract and present the required data
- Accuracy of reports
- Data consistency across systems for master / transaction and historical data
- Real-time support to business processes
- Number of tickets / issues logged
- Data consistency across systems
- Real-time support to business processes
- Impact on customers and other external parties
- Integrated business workflows
- IT Total cost of ownership reduction over time
- Impact on customers
- Rationalized applications portfolio

Key Success factors

- Increased Business involvement with advancement to each stage
- Key entry and exit criteria should be clearly defined for each stage
- User satisfaction survey should be conducted at each stage
- Proactive Project Charter and Governance should be defined well before the formal merger
- The internal IT strategy should aim to integrate, centralize, outsource, and economize
- Power and Politics should be properly managed i.e. more time and money should be spent for BPR and change management
- (Business users, IT users, and budget) should be available for moving from one stage to other stage
- Innovative strategy to retain employees with relevant knowledge is key for integration
Conclusion
The integration of two IT / ERP systems is a complex project, which involves several challenges. The important things to be kept in mind are

- A high degree of integration of the different systems can provide large benefits
- An excellent communication strategy is important
- Maintaining competitive parity in technology usage is essential
- Focus should be on gradual IT Cost reduction

M & A- ERP Application Integration Case Study

Background
Infosys assisted one of the TOP US Bank in its IT / ERP integrating strategy for one of the biggest mergers in banking industry.

After all the events and news of the merger between these two financial institutions, the shareholders and media were keenly looking forward to the 1st Quarter results of the combined entity. The results were also under scrutiny of Auditors and Government. The Bank was successful in producing both the quarterly guidance as well as the financial results on time. This would not have been possible without good systems integration between the two institutions which both individually generate huge financial data on a daily basis.

Transition Milestones I Stages

Legal Day One (LD1) refers to the date the legal closing of the merger transaction and involves least amount of integration required to create a common balance sheet and other key regulatory reporting. Financial Systems like General Ledgers of both the acquired and acquirer runs in parallel and get consolidated in the Acquirers system for common reporting. This is sometimes referred to as Dual Posting. Prior to LD1, the Acquirer & Acquired organizations are considered to be competing companies. LD1 marks the first step toward integrating the two companies into a single organization. This represents Stage 1 of the IT roadmap.

Human Resources conversion would be the day on which the two companies’ Human Resources programs and processes are integrated, including payroll systems and benefits programs. Prior to the Human Resources conversion, associates of both companies would continue using their current Human Resources processes and benefits programs. This represents Stage 2 of the IT roadmap.

Client Day One is the day on which any rebranding efforts would be completed, and the combined company is presented to a specific client segment as a united brand. There can be multiple Client Day Ones depending on the operational readiness of each business unit to serve each client segment as a united brand (including signage, marketing collateral, letterhead, etc.).

Systems Day One is the day on which we would integrate core technology systems and client account databases, and begin to function with a single, combined process. This represents Stage 3 of the IT roadmap.

-Due diligence and Planning

Due diligence and Planning will take most of the effort and is critical. This is what we tried to analyze as shown in the Figure below using our model for this particular case on the banks Financial ERP Applications.
Key Learning’s from the above Case Study

- **Establish an integration strategy that involves the business.**
  These strategies need to be
  - *Short term, for example* to execute the immediate LD1 phase
  - Long term for 18-24 months where first the target system landscape is defined. The total transition is then broken down into various stages and each execution plan defined for each stage

- **Break projects into different streams**
  Adopt the systems/technology which are best for the combined entity and which may not always be one of the latest. In this case the Acquiring Bank’s key financial systems like General Ledgers and sub ledgers were on Mainframe Based systems. These were old systems and had their own functional limitations. However the bank still went ahead with merging and retaining mainframes since it was more cost effective and efficient than reporting out of Oracle financials which the other bank had.

- **Manage People issues:** Like any other business unit, IT Staff would also face insecurities during Merger. Staff skills and hence their jobs are tied to the technology or Software platform which they have been working on. For example, after sunsetting People soft system acquired from merger, many tech folks who had good knowledge on business processes were absorbed in business transformation kind of projects in the Acquiring bank. They were retained though on a different SIW platform
• Establish key parameters to monitor the progress. One of the key parameter is budgets. Various projects which fall under transition are generally on tight budgets and would be forecasted and monitored very closely. Budgeting cycles would be of short period and any un-utilized dollars in a period would be taken away from the project rather than moving it to next period. Other key parameters can be timelines and exit criterion for each project execution stage.

• Consider long term IT strategy & investments already committed / initiated: Now a day's most of the FI's are planning / investing in long term enterprise wide software platform. There can be a conflict between both Acquired & the Acquiring Company having this commitment and on a different S/W platform. Since these are high investment areas, what happens to these implementations after mergers have financial implications?

As an example here, the Acquiring Bank was in the midst of implementing org wide SAP platform when it acquired the other bank which had recently implemented Org wide Oracle Financials. Both banks had invested/committed millions of dollars in these initiatives.

Following critical criterions should be considered while deciding the final system landscape
• Should be able to maintain system availability and minimum business disruption
• Should be able to address the business requirements from Merger
• Reduce overall cost of ownership

Conclusion I Client Decisions

It’s interesting to know in this case, how the Acquiring Bank leveraged best of both the Enterprise systems to achieve maximum Return on Investment.

Since the bank which was acquired had more international presence, the Merged Entity used their ERP systems i.e. Oracle financials for the Merged international operations.

On the other hand, the Bank saw lot of cost & process efficiencies to have one common SAP platform for America's business and decided to move Merged Entity to SAP.

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