Executive Summary

Merger and acquisition (M&A) activity is booming. In 2015, global M&A volume exceeded $4.25 trillion, a new record. Yet the failure rate for M&A deals is alarmingly high—as it has been for decades. A recent Harvard Business Review article said 70–90% of M&A deals are “abysmal failures,” and a survey from Deloitte reveals 90% of executives felt M&A transactions did not generate the expected value or ROI.

What is the explanation for this perpetual chasm between expectations and reality? Many executives point to the complexities of IT integration as the root cause of M&A failure. Industry experts seem to concur, having investigated this topic in countless articles, white papers, and conferences. Yet the high failure rates persist. It’s time to consider a new strategy for M&A success. We need an approach that focuses not on integration itself but on the intended result of integration—in a word, transparency.

Transparency into data, IT assets, operational practices, and business processes—before, during, and after integration—empowers IT to deliver more than “integration” of the buyer and the acquired. It enables IT to deliver benefits at all phases of the M&A process—from arriving at accurate valuations in the due diligence phase to highlighting compliance or integration issues in the planning phase to understanding exactly what IT assets are owned and how to optimize their use in the integration phase.

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1 Source: Statista, 2016.
This information is most vital at the time management is making go/no-go decisions.

Higher transparency can accelerate M&A timelines, impact asset valuations, and influence decision making about whether and when to integrate acquired organizations. Whether your company is interested in higher value from M&A or higher valuations from divestiture, it’s time to place a premium on transparency—of your own processes as well as those of your acquisition targets. This point of view examines how to do that and provides real-world examples to help you explore the possibilities.

**Causes and consequences of the “transparency gap”**

Why do companies merge? For the same reason they do everything else—to maximize business value. Traditionally, M&A has enabled companies to do this by helping them achieve growth targets, minimize risk through diversification, expand their geographical presence, extract costs from operations, diversify their business lines and customer bases, squeeze value out of poorly managed companies, exploit economies of scale, and so on. Today, M&A activity is also aimed at adding new technological capabilities, altering the competitive landscape, or changing the market in favor of the new entity. For example, a recent study by KPMG found that the top five reasons for M&A professionals to initiate a merger or acquisition in 2016 included: entering a new line of business, expanding their customer base, expanding their geographical reach, enhancing intellectual property or acquiring new technologies, and responding to opportunities when a target becomes available.

Similarly, divestiture is aimed at increasing business value by maximizing the valuation of sold assets and minimizing the costs and disruptions of separation. Whether the divestiture takes the form of a straight asset sale, an asset trade, or something more complex, such as a spinoff or joint venture, your organization’s key goal is to surpass book value.

“Divestitures become a lot easier when you have a good service management philosophy. Get your arms around what you have and how it’s used. It’s not sexy, but you need to do it. There is no point in recreating something that is not used or decommissioned.”

– Richard Donaldson, Director of Infrastructure Management and Operations, eBay

Regardless of the specific motivation behind an M&A transaction, it’s impossible to maximize shareholder value and asset valuations without adequate information about the underlying assets. Yet we continue to live with the transparency gap—the difference between the information that’s needed and the information that’s actually available to M&A teams. Perhaps it’s because we haven’t fully considered the consequences of this limited visibility.

Let’s take a closer look at the hidden causes and costs of the transparency gap. Consider a hypothetical example of $10 billion Company A that wants to acquire $5 billion Company B in order to grow beyond its traditional borders. What does Company A care about in terms of business information systems from an M&A perspective, and where does limited transparency create obstacles? The examples below help define the three phases of a typical M&A transaction.

**Due diligence phase**

**Financials**

The acquiring company will want a financial history of the acquisition target, along with current budgets, planned CapEx, an understanding of the purchasing and capitalization process from an IT perspective, where revenue comes from, profitability against cost of sale, ability to meet return-on-sales goals, etc. However, most legacy IT systems do not provide insights into where and why budget is allocated and spent, making it extremely difficult to address any of these information requirements. As a result, inaccurate assessments of everything from asset values to future revenue streams can occur.

**Customers**

To arrive at an accurate valuation, the acquiring company needs a complete understanding of the target’s entire business, including how much it spends, which products it buys, what contracts it has, its terms and conditions, its risks and liabilities, and so on. More than likely, however, customer data is dispersed across the enterprise—in multiple systems that do not share data and cannot be easily integrated. This makes it nearly impossible to extract the complete and accurate customer information that’s essential to financial forecasting.

**Human capital**

The acquiring company needs to know what the target’s organization chart looks like, what skills and expertise employees possess, including the job roles, titles, accreditations, certifications, benefit packages, NDAs and signed contracts. Retaining those experienced employees is also critically important, and creating a positive onboarding experience for acquired employees can determine the success or failure of the M&A transaction. However, most legacy information systems do not provide centralized access to this information. In addition to making it difficult to adequately evaluate HR issues, this lack of transparency contributes to lower-than-expected employee retention rates as companies merge. In fact, Mercer found that 55% of buyers—both corporate and private equity—cited employee retention as the number one perceived risk for merged or acquired companies.

**Intellectual property and goodwill on the balance sheet**

Patents, trademarks, copyrights, and partner agreements have substantial impact on M&A valuations. Yet the vast majority of enterprises struggle with IP tracking, and poor integration across the acquired company makes extracting accurate information a time-consuming, expensive, and often fruitless effort. This can make companies easy prey for vigilant companies looking to capture valuable IP at a low price.

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Integration planning phase

IT asset inventory

The starting point of any planning phase is knowing what resources you have at your disposal. The acquiring company will need a complete and itemized list of which IT assets are owned by the acquisition candidate and how they’re used—as well as which assets may have to be replaced following the acquisition. In addition, companies involved in divestiture need the ability to untangle which core systems are involved in which operations. For example, if a company wants to sell a piece of its business, it needs to know with certainty whether associated IT costs will disappear once the transaction is complete—but shared assets, such as a data center, may leave the divesting company with sunk costs it may not be able to recover.

“Since M&A integration projects usually involve working with systems already in existence, it is important to focus on discovery and analysis of those systems during due diligence while also envisioning the future state of the integration.”

– Cognitive Diligence

All too often today, however, the acquisition target cannot supply anything more granular than a list of hardware, software, and network elements purchased recently. Anything more specific, such as “service mapping” that shows how each asset is actually used in production in performing business processes or delivering business services, is likely to be either unavailable or inaccurate.

Software license compliance

A recent survey by King Research shows that an alarming 69 percent of IT executives are not confident about being compliant with their software licensing agreements—and the consequences of non-compliance can be multi-million-dollar fines. Moreover, companies such as Oracle and Microsoft frequently schedule audits shortly after major mergers or acquisitions, so having some way to quickly determine whether an acquisition target is compliant with their software licenses will easily pay for itself. However, many enterprises cannot perform self-audits in anticipation of an actual divestiture through higher transparency

For companies contemplating divestiture, the key question is how to maximize asset valuations. The answer is having hard data to support higher assessments.

In 2015, the parent company of a major U.S. financial services firm announced a strategic shift that required the divestiture of billions of dollars of commercial assets. Because this company had invested in the systems and processes needed to create transparency for its business operations, it had the data it needed to command higher asset valuations.

Specifically, the company implemented a service management platform that was able to identify—for each business process—all of the elements that support a given business service. With a complete and accurate record of all IT assets and how they supported business processes, the company had accurate data to support higher valuations. Executives have asserted that this level of transparency contributed to higher-than-book-value sales for some of its assets.

audit because they do not have processes and tools in place to ensure that good quality data and an accurate view of compliance are easily accessible on a day-to-day basis. Moreover, many investment bankers lack expertise on the technology side of M&A activities—they don’t know what to look for or expect in terms of the granularity of software license information.

Quality of service

The quality of the services and solutions provided by the acquired company is directly related to customer satisfaction and loyalty, so the acquiring company will want specific metrics pertaining to availability levels, performance, and other quality metrics as well as customer satisfaction metrics, such as the Net Promoter Score (NPS). Unfortunately, most organizations cannot quantify availability and performance levels because their systems and processes are built in a piecemeal manner that leads to incompatibility and lack of transparent information. As a result, changes are difficult and expensive; there is no visibility into which systems can be phased out and where the organization needs additional investments; and capital expenditures may be higher than necessary, creating an easy win for an acquirer that can stop the flow.

Security and compliance

The acquirer will want to know who has access to proprietary code in products and services, regulatory requirements relating to the products and services of the acquired company, alignment with all local laws, how products are physically and logically protected, and so on. These requirements become even more important as the volume of cross-border deals continues to increase. According to Baker & McKenzie, cross-border M&A activity will outpace domestic activity, rising back to a 38% share by the end of 2017. However, rapid and relentless changes in everything from regulatory requirements to security threats and attacks challenge governance risk and control programs and security measures to keep pace. Assessing dependencies across risks, compliance, and cybersecurity issues is extremely complex and time consuming.

Integration phase

According to a 2015 Deloitte study, 60% of executives considered a recent M&A in their firm to be “very unsuccessful” to “somewhat unsuccessful” in terms of the post-merger integration. Clearly, a lack of visibility into vital information from the due diligence and integration planning phases severely limits the efficiency and effectiveness of the actual integration. Contrary to popular belief, this lack of transparency is the actual root cause of the high failure rates of M&A transactions, not the integration effort itself.

Quantifying the impact of IT integration

Not every IT function in an acquired company needs to be merged with the acquirer. Certain pockets of IT within the acquired company may be better off remaining discrete entities. But how does the acquirer determine whether and when it makes sense to integrate them?

CareWorks, one of Ohio’s largest managed care organizations, was acquired by New Jersey-based York Risk Services Group in 2014. Having established a highly effective shared services model, CareWorks had sufficient transparency into operations to propose an innovative solution to the integration conundrum:

Integrate specific IT functions into a common operational shared service platform, baseline those functions against enterprise Service Level Agreements (SLAs) for three to six months, and quantify the impact of integrating them into central IT versus allowing them to remain separate.

For the acquiring company’s risk services group, this approach is now helping minimize the cost and disruption of IT integration in support of multiple acquisitions.

"Using a single solution resulted in accurate compliance rates for help desk services. It got out of the way and let me lead transparently across the globe. The implementation was successful enough that other departments, including facilities operations and HR, are requesting the tool in their own departments.”

– Dave Schecklman,
Chief Information Officer, Oshkosh Corp

Bridging the transparency gap

Now that we’ve established that information and business process transparency are the critical factors to reaping the full benefit of a merger or acquisition, the question becomes how to achieve this. How do you create an IT environment that increases transparency at every phase of M&A? How do you achieve higher visibility into everything from data to IT assets to entire business processes? How do you “own” the process as well as the firm itself?

70% of acquisition targets had compliance issues, and half of them lacked comprehensive data security architectures.”
– CSO.com

And since your business is only half of the equation—after all, the IT of the acquired entity was never within your control—how much of a difference does it really make what actions your company takes to deliver higher transparency?

By taking the steps outlined below, your organization can strengthen its position as both acquirer and acquired and deliver on its primary charter of maximizing shareholder value. By doing so, it can also serve as a model for other organizations and thereby make a direct contribution to a dramatic decrease in the M&A failure rate.
Five steps toward transparency

While the purpose of this paper is not to prescribe any specific solution or technology, it is helpful to begin identifying actions you can take to deliver a higher level of transparency.

1. Put IT on the M&A team

All too often, IT is made aware of M&A or divestiture plans after the deal has already been struck, which guarantees a rocky road for integration. Make sure IT is a full and active participant in every stage of M&A activities.

2. Use a single system of record for IT

Have your IT service delivery, operations, and business users all work from the same system of record, meaning a single, authoritative source of management information. This will enable you to deliver simpler, more reliable services with minimal overhead. Equally important, it will ensure the accuracy of your data about IT assets, which is typically contained in a configuration management database (CMDB). Ultimately your CMDB should serve as a foundation to a “service-aware CMDB” that maps business services to the infrastructure supporting them, allowing for a comprehensive understanding of the services being acquired and the necessary infrastructure to support them. After all, if the accuracy of IT’s information about its own assets can’t be trusted, IT’s ability to supply reliable data to M&A teams is severely compromised. Surprisingly, many firms and large banks still do not have a CMDB or CMDB data they can trust.

3. Transform IT best practices into enterprise best practices

By standardizing on ITIL (Information Technology Infrastructure Library) best practices, you will be able to provide end-to-end visibility into all ITIL-conformant processes and infrastructure through your single system of record. This, in turn, makes it possible to consolidate fragmented tools and legacy systems, integrate data from multiple sources, and automate processes.

4. Manage IT services, not just IT assets

At the most fundamental level, IT is about service delivery, not infrastructure or “plumbing.” By managing IT services from end to end, you increase transparency into every aspect of the business processes served by IT. An added benefit is positioning IT as a true service provider and strategic partner to the business.

5. Extend the concepts of IT service management to every business process

The ultimate goal is to apply the same level of structure, best practices, and consistent service delivery you create for IT to every repeatable business process, including finance, HR, marketing, facilities, legal, and so on. That’s the key to creating the transparency that makes an M&A or divestiture transaction successful.
Learn more

ServiceNow is changing the way people work. With a service-orientation toward the activities, tasks and processes that make up day-to-day work life, we help the modern enterprise operate faster and be more scalable than ever before. Customers use our service model to define, structure and automate the flow of work, removing dependencies on email and spreadsheets to transform the delivery and management of services for the enterprise. ServiceNow provides service management for every department in the enterprise including IT, human resources, facilities, field service and more. We deliver a ‘lights-out, light-speed’ experience through our enterprise cloud – built to manage everything as a service.

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