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Introduction

Mergers and acquisitions (hereafter M&A) have been a popular method for companies to increase or improve operations, acquire new technology or product lines, expand their customer base, penetrate new markets, and achieve greater integration of their supply chains. Unfortunately, about half of M&A ventures fail to produce the desired results (Saari, 2007) (Trautwein, 1990). Acquisitions where the acquiring company and target company are in a related industry tend to be more successful than mergers between firms in unrelated industries whereas about 75% of mergers between unrelated firms fail (Trautwein, 1990). Clearly, there appears to be a problem between making an acquisition or merger and making it work as desired. The problem of M&A failure, however, appears to be mitigated by an effective acquisition plan that helps acquirers avoid factors that negatively impact a venture. When proper due diligence is exercised acquisition related problems may be identified and rationally addressed thereby laying the foundation for a successful transition plan, In addition, an adequate combination of finance instruments can provide the funds necessary to allow the newly formed organization to function without financial duress while managers and employees execute the transition plan in a structure, efficient manner.

Analysis of the Strategic Planning Process

M&A ventures have been a popular method for companies to increase or improve operations, acquire new technology or product lines, expand their customer base, penetrate new markets, and achieve greater integration of their supply chains. Unfortunately, about half of M&A ventures fail to produce the desired results (Saari, 2007) (Trautwein, 1990). Acquisitions where the acquiring company and target company are in a related industry tend to be more successful than mergers between firms in unrelated industries whereas about 75% of mergers between unrelated firms fail (Trautwein, 1990). Clearly, there appears to be a problem between making an acquisition or merger and making it work as desired.

The problem of M&A failure could be mitigated by an effective acquisition plan that helps acquirers avoid factors that negatively impact a venture. An effective plan should have a macro-level approach that addresses salient internal and external factors, as listed in table 1, in order to assist managers in establishing clear goals (Reed, 2007,p.15).

Table 1
Major Elements of an M&A Strategy

Internal Elements	External Elements
• Mission-Vision Statement	• Business Environment
• Core Competencies	• Customers
• Culture	• Competitors
• Core Assets	• Suppliers
	• Alliances

Trautwein (1990) emphasized that in addition to addressing internal and external factors, a strategic M&A plan should be developed relative to the motives of the acquiring company's M&A team and should address the company's corporate-level and business-level strategies as well as the means of acquisition relative to the venture under consideration. These strategies can be focused through application of tools such as the *Wheel of Opportunity/Fit Chart* (hereafter WOFC). The WOFC is used in three basic phases to guide the M&A team in assessing the target's traits that can supplement or complement the acquiring company's traits, weight the complements and supplements relative to their importance, and to rank targets by their ability to maximize the complements and supplements (Reed, 2007, pp. 17-22). In addition to establishing the strategic fit between an acquirer and a target, Jemison (1986) emphasized that performance criteria should be established pre-close in order to set time-based goals. Emphasizing the importance of finding the correct target, Newton (2008) stated, "Since M&A is difficult to undo, companies seeking to grow through this process must be very sure that the target company will be the right fit" p.5.

Effective strategic M&A planning is typified by Well Fargo Corporation and their tactical use of their internal audit department to guide the process. Due to the corporation's large amount of M&A activity, Wells Fargo's executive managers expanded the scope of their internal audit department to include M&A planning activities. Because the internal audit department had intimate knowledge of Wells Fargo's operation, their auditors were well positioned to understand the acquisition motives of their executives and had a skilled staff to assist in finding appropriate targets. In addition, the M&A planning activities formed the foundation of what would become the due diligence process. The benefit to the corporation was that planning costs were low, plans were practical, and the knowledge acquired by the audit staff was retained internal to Wells Fargo, and most M&A ventures were successful (Nygaard, 2002).

Although many firms do not have the benefit of a formal internal audit staff, the Wells Fargo approach to strategic planning emphasises the things that any firm do. These include establishing specific roles for the M&A team, determining the correct fit of a target, setting achievable expectations, and identifying key deliverable items. "With a clear strategy, effectively communicated, well-plannes, and carefully implemented, the chances of superior performance are enhanced immensely," (Creating Strategic Excellence, 2009, p. 1).

Analysis of the Financial Instruments

Financing for M&A ventures can be achieved in various ways but is frequently determined by the type of transaction being considered (Simpson, 2010). Stewart (2006) found that most corporations will take on as much debt as possible rather than equity in order to retain control of the company. Only when the limit is reached of what the debt market will provide will company executives seek other sources of funds. These finance sources may be a combination of debt and equity, loan from a commercial bank, bonds, and commercial paper to an investor, common stock, or a hybrid like preferred stock. In situations where the acquirer is using a debt-equity combination, there may be inadequate debt and insufficient equity to finance the transaction. In this type of situation, the acquirer could issue junk bonds to make up the difference. Reed (2007, p.145) provided a summary of sources of debt and equity that are listed in table 2.

Table 2
Common Sources of Debt and Equity

• Asset Based Lenders	• Insurance Companies
• Commercial Banks	• Investment Banks
• Commercial Finance Companies	• Merchant Banks
• Employees (ESOP)	• Private Investment Firms
• Investment Companies (Mutual Funds)	

Of the common sources of debt and equity, there is evidence that managers prefer debt and cash to equity in order to protect their control of the company (Karpenko & Larratt-Smith, 2007) (Amihud, Lev, & Travlos, 1990). When using multiple layers of debt the instruments are ranked by seniority with the most senior debt being secures by a first lien on the firm’s assets and subordinated debt such as junk bonds or other debt that is either unsecured or secured by a second lien on assets. Warrants are an additional form of subordinated debt and typically allow the holder to purchase stock at a reduced price at a specified future date (Reed, 2007).

There are downside considerations, however, to using a high percentage of debt to finance an M&A transaction. For instance, the more leveraged the company the lower its credit rating becomes thereby restricting the company's ability to secure additional debt if needed and financial ratios may be adversely affected as a result. Long-term debt obligations place a commitment on cash and this obligation has a direct impact on the company's income statement and balance sheet. Another important consideration for highly leveraged transactions is that managers may lose considerable control if the firm goes into bankruptcy thereby defeating their intent of having dominion over the company (Karpenko & Larratt-Smith, 2007).

In the recessionary period since September 2008, it would appear that a company's ability to acquire debt for M&A ventures would be relatively restricted. According to Keener (2009), however, restrictive financing is not hindering M&S ventures providing the acquiring organization has a practical business case and a well-developed acquisition plan.

Analysis of the Due Diligence Process

Due diligence is generally the process of reviewing critical factors that support a process or action. Copeland (2000) provides a comprehensive explanation of due diligence relative to M&A:

> The process of examining the financial underpinnings of a corporation as one of the first steps in a pending merger, equity investment or large-scale IT purchase, with the goal of understanding the risks associated with the deal. (p.1)

The primary deliverable item from the due diligence process is the Due Diligence report and it should address the following broad categories (Nygaard, 2002):

- Open Issues
- Financial Impacts,
- Definitive Agreement Issues
- Transition issues.

The due diligence process should be an extension of the pre-merger plan in that the degree of due diligence depends on the acquirer's primary acquisition motive and the goal of what is expected from the venture in terms of employees, customers, processes, assets, production capacity, general operations, or services (Webster, 1997). Information technology (hereafter IT) presents special considerations to the due diligence process because many M&A transactions fail due to incompatible systems, lack of upward scalability, loss of key IT managers, and issues of intellectual property rights. In addition, pre-acquisition contingencies must be addressed in as much detail as practical. These contingencies include pending litigation, warranty obligations, assessments or tax levies, financial liabilities, pension liabilities, and lease covenants (Newton, 2008).

The acquiring company should create a due diligence team consisting of executive managers, operations managers, accounting, and legal personnel. The team should investigate the target company's financial statements and if it is a public company, review the SEC filings. Additional areas of review include litigation history, UCCs, material agreement, and intellectual property agreements. Many firms contract outside personnel to pursue these activities but large firms can use their internal audit departments. Two such firms, Ameritech (Burke, 2000) and Wells Fargo (Nygaard, 2002) have achieved success in their due diligence efforts while keeping the associated costs low and protecting the business intelligence acquired from the process. The primary advantages of using internal auditors for the due diligence process is that they have intimate knowledge of the acquiring firm's, processes, controls, and culture and will have professional knowledge of where to seek and find details of corresponding areas in the target company. In organizations where M&A activities occur frequently, the internal audit departments can create due diligence templates that may be used to quickly, inexpensively, and accurately gather pertinent information for the due diligence report (Burke, 2000). Properly prepared due diligence reports can eliminate reservations that lenders may have regarding the transaction, become a device to share knowledge between the acquiring and target organizations, and should become the foundation of post-merger implementation plans.

Analysis of Post-merger and Divestitures

Evidence reveals that 60% of all M&A ventures fail (Saari, 2007) (Trautwein, 1990) frequently due to the acquiring firm placing emphasis on cost reduction, product improvements, and economies of scale at the expense of intrinsic aspects such as cultural compatibility, and demotivation of employees (Cartright, 2009). It appears that the perennially high failure percentage of mergers and acquisitions has induced caution in lenders. Consequently, in the business environment of 2010 it is more important than ever for organizations to successfully achieve their M&A objectives. Keener (2009, p.38) states ". . .integration programs that incorporate diligent planning, structured execution, and attention to softer issues such as corporate culture, executive support and talent retention are now recognized as being central to the long-term success of any deal."

It appears that due diligence and post-merger integration are two sides of the same coin and thus complement each other. The financial and operational aspects of a merger as identified in the due diligence phase must be successfully addressed such as integrating accounting and financial systems, manufacturing operations, asset management, sales, and marketing. But the probability of success in these areas increases when employees of the target organization feel they are an integral part of the new company. In fact, 60% of the firms surveyed by Keener (2009) indicate that they intend to change their M&A processes to ensure success; ". . . enhanced integrations processes will be emphasized" p. 39.

"The more strongly employees feel ownership of the strategy, the more they will feel committed to play their part. Ownership, commitment, and involvement begin with a major communications exercise to see that employees fully understand the strategy. . ." (Creating Strategic Excellence, 2009, p4).

Conclusion

Mergers and acquisitions (hereafter M&A) have been a popular method for companies to increase or improve operations, acquire new technology or product lines, expand their customer base, penetrate new markets, and achieve greater integration of their supply chains. Unfortunately, about half of M&A ventures fail to produce the desired results (Saari, 2007) (Trautwein, 1990). Acquisitions where the acquiring company and target company are in a related industry tend to be more successful than mergers between firms in unrelated industries whereas about 75% of mergers between unrelated firms fail (Trautwein, 1990). Clearly, there appears to be a problem between making an acquisition or merger and making it work as desired.

This failure, however, appears to be mitigated by an effective acquisition plan that helps acquirers avoid factors that negatively impact an M&A venture while addressing factors that can assist managers in establishing and following clear goals. In addition, when appropriate financing is acquired, the newly formed organization can enjoy adequate funds to confidently implement the M&A plan through structured execution and attention to softer issues such as cultural fit, executive support, and talent retention.

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(Dieckmann, 2066) (Newton, 2008; Creating Strategic Excellence, 2009) (Saari, 2007)