INSTITUTE FOR GOVERNMENT

Managing at arm's length

Guidance Note 4

Managing mergers of public bodies

Context

This paper focuses on mergers of NDPBs and is intended for Departmental officials and those working in public bodies involved in organisational mergers. The analysis draws on a range of documentary evidence and other written sources, including academic and business literature on mergers; reports from the National Audit Office, Audit Commission, Ofcom, Gatenby Sanderson, Veredus and others on managing public sector mergers in the UK; Select Committee reports and interviews with a number of individuals involved in recent mergers.

Getting mergers right is not easy and most private sector mergers destroy value. In private sector mergers, studies suggest that most failures occur during the integration process. The major causes include "improper managing and strategy, culture differences, delays in communication, and lack of clear vision. Therefore, the keys to successful integration process are a hands-on leadership styles, a bias for action, involvement of the entire staff, continuous focus on the people the body is supposed to be serving, as well as citizens and other interested parties more generally, , and most of all, open and honest communication with employees."[1] It seems likely that similar factors have a significant role to play in determining the success of public sector mergers.

The specific responsibilities of the sponsor team, the wider Department, the bodies being merged and the leadership team of the planned new organisation will reflect the specifics of the situation. In general terms, however, the sponsor would expect to decide the rationale for the merger, craft the legislation required (if relevant), set the financial parameters, make key early appointments, starting with the Chair and, potentially, staffing issues – proposed structure and grading, pay remit and the process for moving staff into the new structures and dealing with those displaced. Second reading is the trigger for being able to make appointments and spend money on the new body. Having appointed a board for the newly merged body and set the parameters for the merger, most of the responsibility for integration of the merging organisations would then pass to them.

Learnings from past mergers suggest the importance of the following elements:

- Clearly defined rationale and end-goal which needs to be well communicated to all staff and needs to be reflected in the new Board and organisation
- Leadership and leadership personalities
- Integration (or personnel, IT, finance etc) need very careful steering, and should be properly resourced

[1] Han Nguyen and Brian H. Kleiner *The effective management of mergers*, Leadership & Organization Development Journal (2003, Vol. 24, Issue 8, pp 447 – 454)

- Early identification of potential stumbling blocks to enable them to be resolved in a timely and cost-effective fashion – these include decisions on pensions, tax status and pay issues
- The new approach must take primacy from an early point to minimise stakeholder uncertainty. Boards of the legacy and the new body are required to work jointly to achieve the overall objective.

What you are aiming for

- Value for money, both in relation to the process costs of merger and the ongoing operational costs, while ensuring that the new body can deliver its objectives effectively.
- Clear and comprehensive milestones for the transition, underpinned by accurate resource and risk analysis and a broadly-based due diligence exercise.
- A leadership team for the new organisation that is equipped both to manage a major change process and steer the organisation into a high performing ‘steady state’.
- Staff and external stakeholders (of the new and legacy organisations) who feel fully informed about the merger process and rationale, have opportunities to feed in their views on its impact and are listened to – even if not always agreed with.
- A strategy and business plan for the new organisations that maximises the benefits of merger and ensures expected synergies are delivered.
- A relationship between the new body and its sponsor Department that is built on shared goals and healthy challenge in both directions.
- A seamless transition between structures to minimise the potential performance dip and disruption and impacts on external parties. This may means keeping legacy bodies in existence for a period after the new body takes over.

Strategy

Take time for good quality strategic thinking early on (both in planning and implementation).

Ensure there is claritybetween the sponsor Department and the new body about the role it is being established to play and how the agenda of the new body fits in with the Department's wider agenda.

Undertake a rigorous cost-benefit analysis of the change before committing to it, and share this with stakeholders. Recognise that there will be some disbenefits to any change, and ensure that these are acknowledged and addressed in planning the transition.

When the decision to merge is taken, establish a set of relevant measurable benefits to be achieved, and collect baseline data before the merger commences. Measure and monitor progress against these objectives.

Clearly identify and account for the costs of carrying out the merger, including setting a separate budget.

The voice of experience

The full extent of the merger costs
The creation of Ofcom was funded by a loan from the Department of Trade and Industry amounting to £56.8 million, but the National Audit Office has calculated the full cost of the merger to be at least £80 million. Policy makers who propose mergers should give serious consideration to these costs in assessing whether a merger will represent value for money.

National Audit Office, *The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies* (July 2006)

Relationships

Agree a Memorandum of Understanding up front between Sponsor Department and legacy Commissions (and between shadow organisation and legacy Commissions if dual running is in operation).

A strong relationship between the new organisation and the sponsor Department offers huge advantages. The incoming leadership team should establish positive common ground with the Sponsor Unit at the very start, to ensure that the inevitable subsequent disagreements can be managed constructively.

Both the sponsor Department and the incoming leadership team of the new body should maintain constant dialogue with stakeholders prior to merger.

Recognise that stakeholders of the legacy organisations will not necessarily be the only or most important stakeholders of the new organisation; take time to identify and engage new stakeholders.

Managing media reaction to the new organisation – and the risk of overt or subtle lobbying against the change by legacy organisations – is essential.

Ensure that Parliament, and especially the relevant Select Committee, is kept informed of merger plans and developments. Respond positively to Parliamentary scrutiny of the merger process and operate as transparently as possible.

The voice of experience

Public face

1. Establish communications functions as soon as possible, even at the risk of depleting the legacy bodies. Media and stakeholder focus begins the moment the Chairman is appointed.

2. Mission statements at an early stage can give internal focus as well as external clarity.

3. Online traffic to the new organisation's website is likely to exceed that to the legacy bodies; ensure there is adequate IS infrastructure in place.

4. Delivery of internal communications should be owned by the new organisation, not the legacy bodies or management consultants. It is unrealistic to expect legacy bodies to proselytise for a new organisation that will be replacing them.

Source: Ofcom, *A case study on public sector mergers and regulatory structures (*May 2006)

Risk

Carry out targeted due diligence as early as possible by gathering important financial, legal, operational and staffing information about the bodies to be merged. This will assist in identifying issues or risks for integration.

Undertake at an early stage a comprehensive review of the actions required to close the legacy bodies, and identify key areas of risk.

Develop the critical path and identify risks early. Ensure there is collective understanding that identifying and actively managing risk is a positive step, not an indicator of failure.

Define accountabilities clearly and monitor them rigorously.

Consider a period of shadow operation for the new organisation rather than an overnight shift from the legacy bodies to the new organisation to minimise risk.

Consider carefully the process of culture change – how much to do in advance of vesting day for the new body and how much to leave for the operation of the new body.

Ensure the launch date for the new organisation is practical and realistic. The critical launch day deliverables must be identified at the outset to allow for effective planning and management of key dependencies.

The voice of experience

How to structure a due diligence programme
One of the most common mistakes in starting a piece of due diligence is to instruct accountants is to instruct accountants, lawyers and other experts and let them get on with it. Every deal is different and so, therefore, is every due diligence exercise. Time spent planning and thinking carefully about what is needed will pay enormous dividends when the programme gets going.

Source: Peter Howson, *Due Diligence: The critical stage in mergers and acquisitions* (2003)

Change management

Decide whether to approach the task as a merger or a ‘start up’, as this will shape much of the planning.

Professional programme and project management needs to be resourced and embedded from the start of the transition process. The role of the Programme Director is critical - both quality and continuity of leadership are important.

A clear and transparent process for stakeholder engagement is an essential part of the transition programme. Stakeholders must be fully engaged and understand the processes and timescales involved in moving any new agenda forward, but should not be allowed to control or constrain that process.

Finance and information systems are complex in all mergers and it is essential to develop a risk mitigation strategy for the integration of finance and ICT. Experienced financial leadership is needed to develop a finance strategy for the whole merger process (including the transition period) and to ensure the establishment of a strong control environment.

Proactive information management and knowledge capture is essential, especially as the programme develops and assumptions change.

Ensure that change management programme addresses the challenge of integrating the cultures of the legacy bodies.

Accept that a process of 'grieving' for the legacy organisations needs to happen. Different people react differently to change but it can often trigger anxiety and a sense of loss. Expectations and fears need to be managed sensitively and realistically.

The voice of experience

How to manage people during mergers

- Develop a good understanding of the two cultures coming together: study engagement data and keep an ear to the ground for insights into what staff are saying.
- Don't assume that leaders of change understand change management. Offer appropriate training to all managers.
- Provide extra support for employees. For example, use confidential "surgeries" run by HR.
- Work closely with the internal communications team from the start.
- Take a regular pulse of employee engagement, sharing the outputs as part of an open and honest approach to communication.

Source: *Put out of joint?* People Management (19 November 2009)

People

Appoint great leaders, and appoint them in the right order. Ideally, appointment of the Chair and then Chief Executive should be completed in time to allow at least a year for detailed planning in the case of complex or contentious mergers.

Ensure the leadership team has a shared understanding of the leadership challenge, their roles in meeting it and the most appropriate style of leadership for the organisation.

The Sponsor Department and. Subsequently, the new leadership team should involve and engage recruitment consultancy support as early as possible, selecting agencies with a track record of working with start-up organisations.

Mergers are a particularly difficult time for staff and a good HR director (permanent or interim) is a vital early appointment. Be aware of the signals that senior appointments make – especially where it appears one body is taking over others. Make sure that the people being appointed are the right ones for the future of the body.

From the beginning of any merger process, attention is needed to a wide range of HR issues and the complexities of TUPE and other aspects of employment law. HR advice should be sought from specialists with experience of public sector mergers, and such advice must be in place before any recruitment starts. Staff transfer and exit schemes are crucial in staff perceptions of the change process. Exit schemes should follow publication of the organisational design, and criteria for selection should ensure that key corporate knowledge is retained.

Identify ‘change champions’ within the legacy organisations and new staff early on.

Regular, frequent, honest and consistent communication is essential to secure the loyalty and commitment of staff to the new organisation. Effective internal communications must also continue beyond launch date, to embed a ‘one organisation’ culture.

The voice of experience

What to look for in a start-up Chief Executive

- Someone who will take the time to invest in their relationship with the Chair/Board from the very outset
- Political acumen and sensitivity
- Ability to work under significant pressure and with a high degree of ambiguity
- A very strong team-worker who will manage upwards as well as downwards
- Someone who is robust on corporate governance and will work closely with the Board on developing this
- An experienced general manager with a broad understanding of the components of a successful organisation: finance, human resources, communications and service provision
- Business skills, flexibility and resilience
- Someone whose skills and experience complement those of the Chair.

Veredus, *Right from the start: lessons learned from the start-up of non-departmental public bodies (*December 2006)

Getting started

The new leadership team should be bold in creating the new organisational identity and values – reinforce cultural change through every aspect of organisational design and development, not just through branding.

Organisational design provides the foundation for other key merger activity, and must be given priority by the incoming leadership team. Sponsor teams should avoid creating organisational designs that bind the new leaders. Plans must be shared with staff as early as possible to maintain the momentum of change and engage staff positively in the process.

Implement a strong corporate governance framework as early as possible.

The new Board should begin with a frank and robust assessment of its capability, and return to this periodically. The Board should discuss, embrace and model the organisation’s core values. This is especially important if there are Board members who were previously involved in legacy organisations – they must be seen by staff and external stakeholders as actively supporting the full agenda of the new organisation.

Mergers of organisations with diverse histories and cultures may benefit from co-location on a new site rather fragmentation across multiple sites. Ministerial commitments to particular locations should be avoided ahead of full options analysis, ideally carried out by the new leadership team.

New leaders in merged organisations should be supported by mentoring from senior individuals who have been involved in similar changes before.

Substantive work on the formal closure of the legacy organisations after the launch date should be managed by a separate team to minimise disruption to core delivery tasks***.***

The voice of experience

Structure and scope

1. Recognise that the type of organisational structure chosen can – if effectively implemented – define the broad approach of the organisation in future.
2. A unitary Board comprising executive and non-executive members of equal status is an effective balancing option.
3. Organisational design should have no sense of obligation to legacy structures and is likely to be designed around the key personnel appointments.
4. A structure designed in theory prior to executive appointments is unlikely to meet practical demands over time.

Source: Ofcom, *A case study on public sector mergers and regulatory structures (*May 2006)

Measuring success

The NAO has developed a measurement framework, or balanced scorecard, for public sector merger structured around five dimensions: strategic objectives of the merger; policy and influence; front-line services; back office services; and people.

Collect data to inform evaluation from the beginning of the transition process.

Review progress regularly. The merger process continues after the formation of the new organisation and phased integration is necessary. Reviews should include processes, structure and management style.

The voice of experience

Degree of success

A review of the literature shows that between 50-80% of private sector mergers disappoint with many destroying shareholder value. This is sometimes due to a lack of strategic fit but more often, it seems to be related to poor post-deal integration. (A global survey by A.T. Kearney in the late 1990's found that 53% of the failures were due to this latter factor, compared to 30% from poor strategy and 17% from how the final deal was negotiated).

We know less about the success of public sector mergers. In part this is because the criteria for success are less obvious but also because, while there are some studies that evaluate individual mergers there has been little attempt to draw general lessons from the experience for the public sector as a whole. Anecdotally it feels like many of the previous reorganisations in health and local government have absorbed a lot of senior management time in return for relatively small public benefit.

Source: OPM, Office *Leading and Managing Mergers: learning from experience* (March 2009)

Where to look for support

Departmental resources: all existing NDPBs should have a senior Departmental sponsor, a 'Fraser figure', who may fulfil this role for several such bodies. Their role should focus on communication, strategic performance management and the allocation of resources. This role is particularly important in a period of change, Departments may also be able to provide support in terms of project and programme planning. Both the sponsor team and the management team of the new body should draw on experience of those who have been involved in mergers – successful and unsuccessful – in departments and NDPBs/

Office for Government Commerce: OGC Gateway reviews are often applied to merger projects once live. One of the lessons from the experience of the creation of the Equalities and Human Rights Commission is the need to take OGC Gateway reviews warnings that projects are off track seriously and not plough on regardless[2]. It is is also valuable to familiarise yourself with OGC's Programmes and Projects Resource Toolkit as part of the planning phase. The OGC website provides access to a range of programme and project management resources, including guides, websites, software and training.

National School for Government: The National School has breadth and depth of experience in all manner of change-related consultancy spanning individual or whole system change; programmes such as Navigating Change (a structured approach to managing change); tools such as the Organisation Design and Change Framework and Toolkit; and training courses designed to develop managers understanding of change management.

Further reading

Audit Commission, *Less dangerous liaisons: early considerations for making mergers work (1995)*
Charity Commission, *Making mergers work: helping you succeed* (September 2009)
CIPD, *International Mergers and Acquisitions: How can HR play a strategic role?* (April 2008)
CIPD, *The impact of mergers and acquisitions on employer brands* (November 2009)

[2] For a description of potential troubles in merging bodies see the Public Accounts Committee *report on the establishment of the Equalities and Human Rights Commission, March 2010 http://www.publications.parliament.uk/pa/cm200910/cmselect/cmpubacc/124/124.pdf*

Don de Camara and Punit Renjen, *The secrets of successful mergers: dispatches from the front lines,* Journal of Business Strategy (2004, Vol. 25, Issue 3, pp 11-14)
Peter Frumkin, *Making Public Sector Mergers Work: Lessons Learned*, IBM Center for The Business of Government (August 2003)
Peter Howson, *Due Diligence: The critical stage in mergers and acquisition (2003)*IDeA, *gearing up for change: preparing for the new unitary councils* (2007)
National Audit Office, *The creation of Ofcom: Wider lessons for public sector mergers of regulatory agencies (*July 2006)
Ofcom, *A case study on public sector mergers and regulatory structures (*May 2006)
Office for Public Management, *Leading and Managing Mergers: learning from experience* (March 2009)
Robert J Thomas*, Irreconcilable Differences,* Accenture (2000)
Veredus*, Right from the start: lessons learned from the start-up of non-departmental public bodies (*December 2006)

This is one of a series of guidance notes on effective arm's length government, developed by the Institute for Government and Professor Matthew Flinders of the University of Sheffield, author of 'Walking without Order: *Delegated Governance and the British State'.*

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