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How to Keep Your Best People During the Ups and Downs of a Deal

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Consider the following scenario. One company signs a definitive agreement to buy another with a two to three month window to close. The financial projections given to the banker depend on the target's completing a particular project, while revenue estimates hinge on retaining key customers at current sales levels. Whatever contingencies are built into the target's financials, the issue facing the buyer remains the same: how to retain employees critical to the newly purchased operation.

We see two common, and equally ineffective, approaches to this issue. Some companies believe they can solve the problem simply by throwing money at people, often without determining who is critical to the organization or identifying their concerns. Too often such companies wind up spending too much on retention programs and key employees leave anyway. Other companies do little or nothing with similar consequences.

Given the uncertainty that typically surrounds a merger or acquisition, companies should not be surprised when competitors try to identify and hire away their target's best people, even in a tight labor market. A flexible retention plan is the best defense against such moves.

Anticipate and Address Employee Concerns From the Start

Timely, honest communication from senior management that anticipates and addresses the concerns of employees at acquired companies can often reduce the ambiguity and anxiety that can cause talented and essential staff to leave. Communications are so critical to making deals successful that savvy acquirers typically have their communications programs ready to launch the day a deal is announced.

Messages from management can take various forms, from personal letters and face-to-face meetings to web-casts. Employees at the target typically want to know why their company is being acquired. They also expect an overview of the acquiring company, its future plans (to the extent these can be shared), how it intends to integrate their company (to the extent this is known), and any changes to their benefits plans. Early messages are a good platform for outlining next steps and what employees can expect in future communications. Frequent communication is important, even when all the details are not known. Every day that passes without a message from the new management team is another day that people speculate, update their resumes, and pursue their own interests, rather than do the work that the company needs and is paying them to do.

Initial steps taken by a media company illustrate just how effective a solid communications program can be. After announcing the acquisition of several television stations in major markets, one of senior management's priorities was retaining a select group of engineers. Management was also concerned that the engineers

might use the uncertainty surrounding the acquisition as an excuse to unionize. The company adopted a very aggressive communication strategy that involved both face-to-face meetings with senior management and frequent written messages both before and after the deal closed. The result was a very high retention rate not only among the engineering group, but also among all employees. And the engineers never tried to organize.

Evaluate Individuals and Prepare Framework

Soon after a deal is announced, business unit leaders from the acquiring company should meet with their counterparts at the target to begin assessing individual employees' technical and leadership capabilities. While the acquirer may have gleaned some of this information from diligence findings, it may be incomplete, given the limited personal contact permitted during most diligence investigations. Assessing key employees' leadership skills is particularly important, for if a "personality leader" were to leave, many others may follow.

In assessing each department, evaluators should place staff into several categories, such as critical to ongoing operations, critical to retain through the close but not necessarily thereafter, highly marketable, and potentially redundant. The integration team should provide training or set guidelines so evaluators avoid rating everyone as "critical," or overlooking key contributors who don't have a manager "going to bat" for them. Categorizing employees in this manner forces managers to evaluate them individually and helps companies determine whether they need to design different retention programs for employees at different levels and locations. When synergies expected from combining the two companies are a primary driver of an acquisition, it may be useful to go through this exercise with the buyer's employees as well.

At this stage, human resources plays a critical role by developing alternative retention plan concepts. HR considers the historical salary of key individuals, along with options and other incentives, in determining what constitutes a meaningful retention award. It is also important to establish some guidelines on how flexible the retention program should be, how it should be implemented and administered, and the challenges it will have to overcome. All individuals may not need the same package, and management should have the flexibility to increase awards for certain contingencies and behaviors. For example, if a department is critical during the first nine months post-close, the acquirer may want to provide smaller individual retention packages with a significant "sweetener" if at least 90 percent of the department stays.

Conversely, if the goal is to allow for orderly downsizing, a successful approach is to provide quarterly retention bonuses. This strategy helped a large energy company retain key employees while it periodically assessed who's "critical," thereby making it easier for the company to shed layers over time in a methodical and cost-effective manner. Through retention bonuses and other targeted awards, the company limited its costs, reached its synergy targets, and made the acquisition succeed. Retention awards can be cash only, stock only, or combinations of cash and stock.

Who Pays?

Once the buyer determines what the retention plan will cost, the next question is who should bear the cost: the buyer, the seller or both? The answer depends on financial yardsticks such as budgeted costs, pro forma synergies, and dollar costs vs. dilution (if an equity instrument is used in the program). An acquirer should consider the tax advantages or disadvantages associated with the final plan design, as well as any employment law implications (EEOC, age discrimination, etc.).

Keep the Messages Coming!

Employee communications can take various forms; however, a personal letter is probably the best way to maintain confidentiality. You might also consider distributing general messages with integration updates and other relevant information. Experience shows that frequent messages are important for reassuring target company employees that their concerns are being addressed. And acquirers should not overlook their own employees. Depending on the framework for the transaction, certain messages may be critical for all employees helping to harmonize cultures and build support for the new business vision.

While this entire process should move ahead rapidly, an overnight fix for retention problems rarely exists. Planning, being flexible and communicating regularly will enhance your company's chances of making its next acquisition a success.

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