Historically, due diligence ("DD") in a merger or acquisition largely focused on the tax and financial consequences of the transaction. An research into the HR implications of the transaction is usually carried out late or after signing. This, while topics related to the (cost of) human capital can have a material impact on the transaction price. In addition, there is the risk of complications during the integration of HR units of the two companies. In some cases this may even lead to potential deal breakers, which are crucial to identify in an early stage.

In this article we highlight the most important points of attention within an HR DD. These points for attention are divided into three subcategories – financial, corporate culture and structural.

Financial considerations
In a transaction there is a risk of future cost increases related to personnel. These costs can be one-off, but also more structural in nature. Examples of one-off costs are severance payments, retention payments, agreed bonuses upon completion of the transaction, or costs related to the HR integration. Examples of structural employee-related cost increases are: structural salary increases in accordance with the collective labor agreement, integration of two different salary structures, or a desired harmonization of the employment conditions. Employees will generally not accept a decline in their terms of employment. A harmonized employee benefit package of may therefore result in an increase in costs.

In addition, employee-related obligations will be transferred to the new company in a transaction. This may be commitments with regard to the pension schemes, jubilee schemes or entitlements in relation to long-term leave.

It is important to include the above financial elements in the financial transaction model in order to get an unbiased picture of the current situation and cost developments in the coming years.

Corporate cultural considerations
One part of the broader company structure is corporate culture. During an HR DD, the culture of the two companies can be examined by means of a quick scan to identify any risks with regard to integration so that the required attention can given to this shortly after signing. A conflict may arise if the companies have a different leadership style (e.g. more or less hierarchical), are different in their willingness to change, or if the decision-making process takes place in different ways.

In addition, it can be researched to what extent employees are willing to contribute to the integration of the two companies and how this involvement can be increased. It is very important that there is sufficient support among the employees, who are actually experiencing the integration of the two companies, to facilitate the transition. By identifying and, if possible, aligning the culture of the two companies, the risk of staff departure can be limited and the identified synergy benefits can be materialized more easily. In addition to an analysis of the company culture, it is often desirable to identify personnel with an important (and indispensable) role. This could be management or employees with particular expertise who are critical to the company’s operations. The loss of these employees in a key role can be a major risk.

By creating certain (financial) incentives related to the transaction, this risk can be reduced or mitigated.

Structural considerations
In a merger or acquisition, two different business structures must be integrated. During an HR DD, it is examined how the various activities are divided within the organizations, how coordination takes place, how this can best be integrated and where any synergies can be achieved.
Employee representation, in the form of a works council or trade union, may have a major impact on future changes in terms of employment. It is therefore important to map out the influence of the employee representation on this process and also to identify what extra-statutory rights are in place. For example, does the employee representative body have extra-statutory right of consent or does the employee representative body have the right to re-discuss certain employment conditions in the event of a merger or takeover?

In addition, there is the functioning of the HR function itself within the newly formed company. In the event of a merger or acquisition, two HR systems and HR organizations may have to be integrated. While the urgency of a strategic HR policy may not be crucial for the survival of the company from day 1. However, it is crucial that the daily HR operations, including systems, are operational from the very first moment.

Conclusion
We consider the early involvement of subjects related to the human capital of a company as an essential part of a DD and of great added value to facilitate a successful transaction. To get a complete picture, we consider financial, cultural, structural and operational aspects. The combination of these aspects provides a complete overview of the risks and opportunities and puts people at the center of one of the largest change processes of a company.

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